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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
*Debtor.*

CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,
*Petitioner,*

against

IRVING TRUST COMPANY, as trustee of the estate of the above-named Debtor, *et al.*,
*Respondents.*

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

## BRIEF FOR PETITIONER.

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# INDEX


| | PAGE |
|---|---|
| Opinions Below | 1 |
| Jurisdiction | 1 |
| Statement of the Case | 2 |
| (a) Facts | 2 |
| (b) Statute Involved | 3 |
| (c) Rulings of the Courts Below | 5 |
| (d) Questions Presented | 6 |
| Specification of Errors | 6 |
| Summary of Argument: | 7 |
| POINT I—The petitioner's claim is allowable, whether or not under the applicable state law the lease was terminated by the landlord's restoration and reletting after rejection but before the enactment of Section 77B | 8 |
| (a) Background and Legislative History of the Statute | 10 |
| (b) Rejection After Section 77B | 14 |
| (c) Rejection Prior to Section 77B | 21 |
| (d) If the Construction of the Court of Appeals be Adopted, the Rejection Provision, as Applied to Prior Rejection, Is Rendered Practically Meaningless. Moreover, Grossly Inequitable Results Would Follow | 25 |
| (e) The Statute Does Not "Create" a Substantive Right | 30 |
| POINT II—There are no doubts as to the constitutionality of the statute which can influence its interpretation | 33 |
| (a) The language of the statute is clear and unambiguous | 33 |
| (b) No question as to the constitutionality of the statute has been raised in the case at bar; none of the respondents was in a position to question its constitutionality | 36 |
| (1) As to creditors | 36 |
| (2) As to the debtor and its stockholders | 38 |
| (c) Even if the debtor or its stockholders could have attacked the constitutionality of the statute, general principles of constitutional law would support its validity | 39 |

PAGE

POINT III—Under the law of New Jersey the liability of the debtor under the lease survived restoration and reletting of the premises ..... 43

(a) Reletting After the Tenant's Abandonment of the Premises Does Not Effect a Surrender Under the Law of New Jersey ..... 45

(b) Restoration of the Premises, Whether or Not Followed by Reletting, Does Not Effect a Surrender Under the New Jersey Law ..... 47

POINT IV—The Court of Appeals committed reversible error in affirming on the ground that the landlord restored the premises, for in so doing it decided an issue not raised either by the pleadings or the proof ..... 52

Conclusion ..... 58

Appendix A ..... i

CITATIONS

Cases:

*Agate* v. *Lowenbein*, 57 N. Y. 604 ..... 48n
*Albrecht* v. *Thieme*, 97 N. J. L. 103, aff'd. 98 N. J. L. 249 ....46, ii, iii
*Auer* v. *Hoffman*, 132 Wis. 620 ..... 45n

*Banks* v. *Berliner*, 95 N. J. L. 267 ..... 46, 49, ii, iii
*Block* v. *Bell Furniture Co.*, 111 N. J. Eq. 551, 559 ..... 49
*Brooklyn Mining Co.* v. *Miller*, 227 U. S. 194, 201 ..... 56n
*Bumiller* v. *Walker*, 95 Oh. St. 344 ..... 45n

*Campbell* v. *Alleghany Corp.*, 75 F. (2d) 947, 955, cer. den. 296 U. S. 581 ..... 39
*Central Trust Co.* v. *Chicago Auditorium*, 240 U. S. 581 ..... 12
*City of Chelsea* v. *Dolan*, 24 F. (2d) 522 ..... 25, 38
*Compania General* v. *Collector*, 279 U. S. 306 ..... 55
*Continental Bank* v. *Rock Island Ry.*, 294 U. S. 648, 670 ..... 40

*Dolton* v. *Sickel*, 66 N. J. L. 492, aff'd. 68 N. J. L. 731 ..... 46, iii

*Emerson* v. *Castor*, 236 Fed. 29, 33 ..... 25
*Ex Parte Blake*, 11 Ch. Div. 572 ..... 15
*Ex Parte Corbett*, 14 Ch. Div. 122 [1880] ..... 15
*Ex Parte Leather Sellers Co.*, 3 Morrell 126 (Q. B. D. 1886) .... 15
*Ex Parte Llynvi Coal & Iron Co., In re Hide*, L. R. 7 Ch. App. 28 15
*Ex Parte Walton*, 17 Ch. Div. 746 [1881] ..... 15

*Fink* v. *Brown Co.* (N. J. Ch.), 99 A. 926 ..... 47, 48, 49n

*General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200 ...55, 56
*Gray* v. *Kaufman Dairy & Ice Cream Co.*, 162 N. Y. 388 ..... 43

PAGE

*Great Falls Mfg. Co.* v. *Attorney General*, 124 U. S. 581..... 38
*Guy* v. *Gould*, 126 Kan. 25..... 45n

*Hanover National Bank* v. *Moyses*, 186 U. S. 181..... 40
*Hardy* v. *Fothergill*, L. R. 13 App. Cas. 351 (House of Lords, 1888)..... 15
*Helvering* v. *City Bank Farmers Trust Company*, 296 U. S. 85, 89 32
*Helvering* v. *Salvage*, 297 U. S. 106..... 55

*In re Carruthers*, 15 Reports 317, 2 Mansons 172 (1895)..... 15
*In re Frazin, et al.*, 183 Fed. 28..... 28
*In re Hyams*, 93 L. J. Ch. 184 [C. A. 1923]..... 15
*In re Metropolitan Chain Stores*, 66 F. (2d) 485, 487..... 53n
*In re Mullings Clothing Co.*, 238 Fed. 58..... viii
*In re Paramount Publix Corporation, Greenberg* v. *Paramount Pictures, Inc.*, 85 F. (2d) 42, 44..... 32n
*In re Paramount Publix Corp. (Madison-Toledo Co.* v. *Paramount Pictures, Inc.)*, 85 F. [2d] 83....9, 17, 21, 24, 25, 31n, 43, 45n
*In re Reiman*, 20 Fed. Cas. 490, 496..... 40
*In re United Cigar Stores Co. (Kuehner and Fischer, Appellants)*, 85 F. (2d) 35.....17, 21, 22, 23, 27, 31
*In re United Cigar Stores Co. (Appeal of Otis Estate Land Trust)*, 83 F. (2d) 202.....16n, 34, 57
*In the Matter of Edward Klein*, 42 U. S. 277..... 40
*Irving Trust Co.* v. *A. W. Perry, Inc.*, 293 U. S. 307..... 10

*J. C. Meyer & Co.* v. *Smith*, 33 Ark. 627..... 45n
*Jones* v. *Rushmore*, 67 N. J. L. 157..... iv

*Kinney Realty Co.* v. *Salmon*, 106 N. J. Eq. 389..... 48n
*Kothe* v. *R. C. Taylor Trust*, 280 U. S. 224.....10, 40
*Kutschinski* v. *Thompson*, 101 N. J. Eq. 649, 660..... iii

*Liberty National Bank* v. *Bear*, 265 U. S. 365..... 55
*Liskovsky* v. *Blau*, 114 N. J. L. 324.....43, 46, 49, i, vn, vii
*Loeb* v. *Columbia Township Trustees*, 179 U. S. 472, 490..... 39
*Lorenz* v. *McCloskey*, 135 Atl. 350..... iv
*Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555..... 40

*McNeill* v. *Town of Andes*, 40 Fed. 45..... 56n
*Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320.....10, 14n, 20, 31, 40
*Marshall* v. *John Grosse Clothing Co.*, 184 Ill. 421..... 45n
*Martin* v. *Siegley*, 123 Wash. 683.....45n, viii
*Maryland Casualty Co.* v. *Beebe*, 54 F. (2d) 743, 746..... 57
*Massachusetts Bonding & Ins. Co.* v. *Santee*, 62 F. (2d) 724, 728 (C. C. A. 9)..... 57
*Meeker* v. *Spalsbury*, 66 N. J. L. 60.....46n, 48, 49n, 55n, iv
*Miller* v. *Benton*, 55 Conn. 529.....45n, viii
*Miller* v. *Dennis*, 68 N. J. L. 320..... 46n
*Miller* v. *Irving Trust Co.*, 296 U. S. 256..... 10

PAGE

*Moore Ice Cream Co.* v. *Rose*, 289 U. S. 373.....22, 35
*Moriarty* v. *City of New York*, 132 App. Div. 10, 12, aff'd 197 N. Y. 544..... in

*Norman* v. *B. & O. R. Co.*, 294 U. S. 240..... 41
*Northern Pac. R. R. Co.* v. *Boyd*, 228 U. S. 482..... 11n

*O'Neil* v. *Pearse*, 87 N. J. L. 382, aff'd, 88 N. J. L. 733.....43, 46n

*People* v. *Knapp*, 230 N. Y. 48, 60..... 39
*Possart* v. *Irving Trust Co.*, 69 F. (2d) 807..... 53n

*Ralph* v. *Deiley*, 293 Pa. 90..... 45n

*St. Louis Casting Co.* v. *Prendergast Const. Co.*, 260 U. S. 469.. 38
*Schmertz Wire Glass Co.* v. *Continuous Glass Press Co.*, 216 Fed. 828..... 56n
*Scott* v. *Beecher*, 91 Mich. 590..... 45n
*Sessinghaus* v. *Knocke*, 127 Mo. App. 300..... 45n
*Shalet* v. *Klauder*, 34 F. (2d) 594..... 43
*Sypherd* v. *Myers*, 80 N. J. L. 321.....47, iv

*Thomas* v. *Matthiessen*, 232 U. S. 221, 236..... 57
*Thorley* v. *Pabst Brewing Co.*, 179 Fed. 338, 339..... v

*United States* v. *Bankers Trust Co.*, 294 U. S. 240, 294..... 41
*United States* v. *Davison*, 1 F. (2d) 465, 469, 470..... 56n
*United States* v. *Illinois Surety Co.*, 226 Fed. 653, 664 (C. C. A. 7)..... 57
*Utah Consolidated Lighting Co.* v. *Apex Mining Co.*, 285 Fed. 249, 256, cer. den. 261 U. S. 617..... in

*Wall* v. *Parrot Silver & Copper Co.*, 244 U. S. 407..... 38
*Whitcomb* v. *Brant*, 90 N. J. L. 245.....46, ii, iiin, iv, vi, vii
*William Filene's Sons Co.* v. *Weed*, 245 U. S. 597..... 14n
*Woolworth Co.* v. *Nelson*, 204 Ala. 172..... 48n

*Yoders* v. *Township of Amwell*, 172 Pa. St. 447, 459..... in

*Zabriskie* v. *Sullivan*, 80 N. J. L. 673, aff'd. 82 N. J. L. 545.... 49

STATUTES, LEGISLATIVE BILLS, AND COMMITTEE REPORTS:

Bankruptcy Act, §63(a), 48 Stat. 911, 923.....13n, 29, 28n, 31n
Bankruptcy Act, §77B, 48 Stat. 911.....3, 13, 18, 20n, 21
76 Cong. Rec. 1360..... 11
78 Cong. Rec. 8109..... 13
H. R. 5884, 73d Cong., 1st Sess., Print of June 2, 1933, p. 10.....11, 12n, 35
Judicial Code, §240(a), 43 Stat. 938..... 1
4 and 5 Geo. V, c. 59.....14, 14n
32 and 33 Vict., c. 71.....14, 14n
46 and 47 Vict., c. 52.....14, 14n

## TREATISES AND LEGAL PERIODICALS:

PAGE

Douglas and Frank, Landlords' Claims in Reorganizations, 42 Yale L. J. 1003 ..... 11
Keegan, Rights of Landlord and His Bankrupt Tenant, 21 A. B. A. J. 379 ..... 21
Schnebly, Operative Facts in Surrenders, 22 Ill. L. R. 117, 129 50
Schwabacher and Weinstein, Rent Claims in Bankruptcy, 33 Col. L. R. 213 ..... 11
Smith, Chain Stores and the Lease Plague, 58 Financial World, 367 ..... 10
Tiffany, Landlord and Tenant, p. 1338 ..... 45, ivn
Tiffany, Real Property, p. 1586 ..... 45
2 Univ. of Chic. L. R. 629 ..... 21
7 Univ. of Cinn. L. R. 164 ..... 11
3 A. L. R. 1080 ..... 45
13 L. R. A. (N. S.) 398 ..... 45
7 R. C. L. 1003 ..... in
16 R. C. L. Sec. 672 ..... 45

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## BRIEF FOR PETITIONER.

### OPINIONS BELOW.

The only opinion below officially reported is that of the Circuit Court of Appeals for the Second Circuit, which is reported in 83 F. (2d) at page 209. The District Court opinion appears in the record at page 49.

### JURISDICTION.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925. The order for mandate of the Court of Appeals was entered April 13, 1936 (R. 74). The petitioner's petition for rehearing was denied by the Court of Appeals by an order entered May 21, 1936 (R. 75, 83). The petition for certiorari was filed August 6, 1936, and granted October 26, 1936.

## STATEMENT OF THE CASE.

This case involves the allowability in proceedings under Section 77B of the Bankruptcy Act of the claim of a landlord "for injury resulting from the rejection" of her lease prior to the enactment of Section 77B by the trustee of the debtor's estate in a bankruptcy proceeding in which reorganization proceedings subsequently were instituted.

### (a) *Facts.*

The petitioner's assignor, Florence H. Bugbee,[1] leased to the debtor, United Cigar Stores Company of America, premises situated in Trenton, New Jersey, for a term commencing April 1, 1926, and expiring March 31, 1946 (R. 23). On August 29, 1932, the debtor filed a voluntary petition in bankruptcy, was adjudicated a bankrupt, and abandoned the premises. At the time of bankruptcy a portion of the premises had been sublet by the debtor. On November 11, 1932, Irving Trust Company, the trustee in bankruptcy of the debtor, rejected the lease and abandoned the premises. After rejection of the lease, the landlord, without notice to the debtor, relet various portions of the premises to the subtenants in possession, and later let certain portions to new tenants (R. 19, 33).

No release or assignment agreement such as is involved in *Meadows* v. *Irving Trust Co.* (No. 151) or in *Otis* v. *Irving Trust Co.* (No. 436), or of any other kind, was executed by the landlord at any time.

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[1] Florence H. Bugbee assigned her claim against the debtor to the petitioner as Agent for the Landlords' Protective Committee in these proceedings.

On June 9, 1934, while the bankruptcy proceeding of the debtor was still pending, the debtor filed its petition under Section 77B in such bankruptcy proceeding, as permitted by the statute.

The petitioner in due course filed a proof of claim (R. 3) for injury resulting from the rejection of the lease. Irving Trust Company, which had been appointed trustee of the estate of the debtor in the reorganization proceedings, objected to the claim on the ground that the lease, which contained no special covenant for damages or indemnify, had been terminated by the landlord's *reentering and reletting the premises* after rejection of the lease (R. 14).

Although the two stipulations of fact which constitute the only evidence submitted to the Special Master, to whom the claim was referred by the District Court for consideration and report, do not contain any reference to the landlord's restoration of the premises prior to reletting, or to her filing of a claim in the prior bankruptcy proceeding for the expense of such restoration, the Special Master, *sua sponte*, stated in his report (R. 41) that the landlord had *filed* in that bankruptcy proceeding "*a claim* for $1,980.99 for alleged expenditures in restoring a party wall and in closing up a common entrance in the demised premises".

(b) *Statute Involved.*

The pertinent provisions of the Corporate Reorganizations Act, which was added to the Bankruptcy Act as Section 77B thereof by the Act of June 7, 1934, 48 Stat. 911, are:

Subdivision (a):

> "Any corporation which could become a bankrupt under Section 4 of this Act, * * * may file an original petition, * * * in any proceeding pending

in bankruptcy, whether filed before or after this section becomes effective, * * *."

Subdivision (b) (10):

"* * * The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts, securities, other than stock, liens, or other interest of whatever character. * * *

"In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: * * *"

Subdivision (p):

"This section shall take effect and be in force from and after the date of the approval of this amendatory Act and shall apply as fully to debtors, their stockholders and creditors, whose interests or debts have been acquired or incurred prior to such date, as to debtors, their stockholders and creditors, whose interests or debts are acquired or incurred after such date. Proceedings under this section may be taken in proceedings in bankruptcy which are pending on the effective date of this amendatory Act."

(c) *Rulings of the Courts Below.*

The Special Master recommended that the claim be disallowed (R. 37) on the ground that Section 77B "could not and did not create any valid and legal claims against the debtor where none existed prior to the enactment of said Section", and that none existed at the time of the enactment of the statute because the landlord's *reentry and reletting* of the premises had effected a surrender of the lease under the New Jersey law. The master's report was confirmed by the District Court (R. 49, 53).

The Court of Appeals affirmed the disallowance of the claim, holding (R. 71) (1) that injury resulting from rejection of the lease for which a claim is allowable under Section 77B must be "recoverable damages" to which the claimant would be entitled under the applicable state law, and (2) that it was impossible for the petitioner to show that the landlord had "sustained any damages from injury by the rejection of the lease" because, *although under the law of New Jersey the landlord's reentry and reletting of the premises alone had not effected a surrender of the*

*lease,*[1] a surrender had been effected by the landlord's restoration of the premises to the condition they were in at the commencement of the term.[2]

(d) *Questions Presented.*

(1) Was the petitioner's assignor a "person injured" by the rejection of her lease within the meaning of Section 77B, and is the petitioner's claim accordingly provable herein, whether or not under the applicable state law the restoration of the premises and reletting effected a surrender of the lease before the enactment of Section 77B.

(2) Upon abandonment of the premises by the debtor, did the restoration of the premises "to the condition they were in when leased" and reletting by the landlord without notice to the debtor effect a surrender under the law of New Jersey?

(3) If so, did the Court of Appeals nevertheless err in so holding when the stipulations of fact on which the case was submitted did not mention that the premises had been restored and the question as to the effect of the restoration was not raised by the trustee's objection to the proof of claim?

**SPECIFICATION OF ERRORS.**

The Court of Appeals erred:

(1) In holding that the petitioner's claim was prop-

[1] The rule in New Jersey in this respect is different from the rule at common law and that in effect in New York and some other states (see *infra*, p. 45).

[2] As the statement of facts, *supra*, states, the record did not show that the landlord had restored the premises prior to reletting. *Even the Master's report did not state that the landlord had restored the premises* (R. 41). Moreover, as stated, the trustee's objection to the claim had raised no issue as to restoration.

erly disallowed because the debtor's liability on the lease had been terminated by a surrender under the applicable state law prior to the enactment of Section 77B;

(2) In holding that the debtor's liability on the lease had been terminated under the law of New Jersey by the landlord's restoration and reletting of the premises after their abandonment by the debtor;

(3) In basing its affirmance on the landlord's restoration of the premises when neither the pleadings nor the proof raised any issue as to such restoration; and

(4) In failing to reverse, with instructions to allow the claim in the amount of any loss that should be proved to have been incurred.[1]

## SUMMARY OF ARGUMENT.

The petitioner's claim is allowable whether or not under the applicable state law the lease was terminated by the landlord's restoration and reletting after rejection in the prior bankruptcy proceeding but before the enactment of Section 77B. The language and the background and legislative history of the statute make it clear that Congress intended to grant relief to all landlords whose leases were previously rejected, entirely irrespective of whether or not their reoccupation or reletting of the premises terminated their leases under the technical law of landlord and tenant of the respective states. From the practical

[1] The two stipulations of fact (R. 19, 33) reserved for future determination the question of the amount of the damages suffered in the event that the claim should be held to be provable.

point of view, such action on the part of landlords had the effect of simply mitigating their loss.

The meaning of the statute is so clear that supposed doubts as to its constitutionality cannot possibly influence its construction. Besides, there are not sufficient doubts as to its constitutionality to influence its construction.

But whether or not the statute is construed in the manner mentioned, the petitioner's claim is allowable, since under the law of New Jersey the liability of the debtor on the lease survived restoration and reletting of the premises.

Finally, since the Court of Appeals committed reversible error in affirming on the ground that the landlord restored the premises, when no issue as to *restoration* was raised either by the pleadings or the proof, in the view of the case least favorable to the petitioner there must be a reversal with instructions for a new trial.

## POINT I.

**The petitioner's claim is allowable, whether or not under the applicable state law the lease was terminated by the landlord's restoration and reletting after rejection but before the enactment of Section 77B.**

As we shall show, the liability of the debtor on the lease did not terminate under the New Jersey law. But if we are wrong in this contention and the debtor's liability is held to have been terminated, it will be because of the trifling and fortuitous circumstances that the landlord, in order to put the premises in a rentable condition, restored a wall and closed a common entrance. Those two acts, according to the

decision below, deprived her of the right to participate in the reorganization of the debtor.

It would seem that a conclusion based on so narrow a ground would have resulted only from a compelling reason such as a clear mandate in the wording of the statute or a plain legislative intent found in the background or history of the enactment. On the contrary, as we shall presently show, that background, history and text clearly require the opposite conclusion. Before doing so it may be helpful to point out what would have been the situation if the landlord had not restored the wall and closed the common entrance.

If perchance when the trustee in bankruptcy rejected her lease the premises had been entirely sublet, she could, according to the court below, have collected the subrents and would still be entitled to prove a claim. *In re Paramount Publix Corp.* (*Madison-Toledo Co.* v. *Paramount Pictures, Inc.*), 85 F. (2d) 83. If, at the time of rejection, the premises had not been sublet and the landlord had reentered and relet the premises without restoring the wall and entrance, she would, according to the opinion below, be entitled to prove a claim. So, merely the fortuitous circumstances that the premises were not entirely sublet and that it was necessary to make some restoration in order to relet them have placed the landlord outside the pale of persons to be benefited, though the result of her acts as a practical matter merely served to mitigate her damages and establish the present rental value of the property.

That, far from intending any such result, Congress intended to give a standing in reorganizations under Section 77B to all landlords who had been injured by the epidemic of tenant bankruptcies, irrespective of

any intricacies and technicalities of real estate law in forty-eight different jurisdictions is clearly apparent from the background, history, and language of the enactment.

(a) *Background and Legislative History of the Statute.*

Under the decisions of this Court, no landlord's claim for damages for loss of future rent was provable under the Bankruptcy Act as it existed prior to its amendment by the Act of June 7, 1934, except a claim based on a lease containing a liquidated damage clause which became operative before or *ipso facto* upon the filing of the tenant's petition in bankruptcy. *Manhattan Properties, Inc.*, v. *Irving Trust Co.*, 291 U. S. 320; *Miller* v. *Irving Trust Co.*, 296 U. S. 256; *Kothe* v. *R. C. Taylor Trust*, 280 U. S. 224; *Irving Trust Co.* v. *A. W. Perry, Inc.*, 293 U. S. 307.

Landlords' claims were held non-provable because too contingent. The contingent character of such claims resulted from the applicability to such claims of the law of landlord and tenant instead of the doctrine of anticipatory breach ordinarily applied to executory contracts relating to personalty. The latter doctrine not being applicable, the landlord had no cause of action for *damages* as for an entire breach, and the amount of the tenant's liability for *future rent* was uncertain in view of the fact that reentry under the general law of landlord and tenant in effect in the various states had the effect of terminating the tenant's liability for rent.

This doctrine of non-provability of landlord's claims under the old Bankruptcy Act was taken advantage of by chain store corporations which were desirous of ridding themselves of obligations under burdensome leases, to such an extent as to become almost a national scandal. Smith, Chain Stores and the Lease

Plague (1932), 58 Financial World, 367; Douglas and Frank, Landlords' Claims in Reorganizations, 42 Yale L. J. 1003; Schwabacher and Weinstein, Rent Claims in Bankruptcy, 33 Col. L. Rev. 213-4; 7 Univ. of Cinn. L. Rev. 164-5. These corporations sought bankruptcy not for liquidation but for reorganization.[1] The members of Congress must have been familiar with this general situation. Indeed, the attention of the members of the House was called to it by Representative Celler in January, 1933, on the floor of the House (76 Cong. Rec., Pt. 2, p. 1360).[2]

The old rule of non-provability obviously was not adapted to a bankruptcy statute which had as its aim reorganization instead of liquidation for, if the claim were not provable, the statute could not constitutionally discharge the reorganized company from its obligations under the lease. Accordingly, Section 77B as first passed by the House provided for provability of landlords' claims in the following language (H. R. 5884, 73d Cong., 1st Sess., Print of June 2, 1933, p. 10):

> "In case any executory contract shall be rejected, the same shall be deemed to have been breached and the holder shall be entitled to file a claim for damages for such breach and such claim may be allowed *provided such contract shall not have been terminated by forfeiture, reentry or otherwise.*" (Italics supplied throughout this brief unless otherwise stated.)

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[1] While landlords were entitled to the protection of the rule in *Northern Pac. R. R. Co.* v. *Boyd*, 228 U. S. 482, various methods of circumventing the rule were available in the absence of a vigilant and well financed opposition.

[2] Mr. Celler said, among other things, that the debtor in the case at bar was one of the solvent chain store corporations that had resorted to bankruptcy for such purpose. Although the record is silent with respect to this subject, it is significant that the debtor filed a voluntary petition under Section 77B two days after it was enacted.

The intent of this provision apparently was to make applicable to leases the doctrine laid down by this Court in *Central Trust Co.* v. *Chicago Auditorium*, 240 U. S. 581, with reference to executory contracts other than leases,—that is, to make the filing and approval of a petition under that bill followed by rejection of the lease an anticipatory breach for which *damages* could be proved. However, (1) the provision was applicable only to a *rejection after the enactment of the bill;* and (2) termination of the lease by the landlord by reentry or otherwise *prior to the hearing on his claim* would defeat the claim even though the termination should not occur until after such a rejection.[1] The effect of the *provision in the House bill, therefore, would have been to bar landlords who had terminated their leases by reentry or otherwise prior to the enactment of the bill* (or who should terminate thereafter but prior to hearings on their claims), and to enhance the amount of claims of landlords who did not terminate before the date of hearings on their claims, to the extent of the rent accruing in the period intervening between rejection and allowance of the claim.[2]

The unreasonableness of such a provision was apparent to the Senate Committee on the Judiciary, and upon its recommendation the Senate on May 2, 1934, amended the provision by substituting in place

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[1] Naturally read, the proviso clause limits the clause "and such claim may be allowed".

[2] Even under the provision of the House bill, however, termination of the lease by the landlord *after* the allowance of his claim would not have resulted in a subsequent disallowance. Aside from the many other reasons mentioned *infra* in discussing the effect of the provision as finally enacted, which are equally applicable to this provision, this is clear from the fact that the proviso clause itself refers only to termination *prior* to allowance of the claim,—"*shall not have been* terminated".

thereof (78 Cong. Rec. 8109) a provision reading substantially the same (so far as now material) as the form in which 77B was enacted, which is as follows:

> "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor."[1]

This provision differs from the provision in the House bill in that the former is expressly applicable to rejection *prior to the enactment of the statute* and does not contain the proviso clause conditioning allowability upon failure to terminate prior to the date of the hearing on the claim (see discussion *infra*, pp. 32, 21). The only reasonable inference deducible from this legislative history is that under the provision as enacted the date of rejection in a prior bankruptcy proceeding is made the effective date of the anticipatory breach of the lease and that termination of the lease thereafter, whether by reentry or surrender by operation of law, is entirely immaterial.[2]

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[1] Section 63(a), which defines the claims which are provable in ordinary bankruptcy proceedings, was also amended by the Act of June 7, 1934, to make landlords' claims provable to a limited extent (48 Stat. 923).

[2] In its brief in opposition to the petitioner's application for certiorari (Appendix B thereof), the trustee argued that the provision in the House bill had to be discarded because (1) the effect of the proviso clause might have been to bar a claim based on a covenant for damages or indemnity, and (2) "the original

### (b) *Rejection After Section 77B.*

Since the person made a creditor by the rejection provision of 77B is one *injured* by a rejection either before or after the enactment of the statute, without any distinction between the two, a brief consideration of the meaning and effect of the provision as applied to rejection after the enactment of the statute cannot fail to be of assistance in determining its meaning and effect as applied to a rejection prior to its enactment.

The landlord provisions of Section 77B obviously were patterned on the English bankruptcy acts [32 and 33 Vict., c. 71, Sec. 23 (1869); 46 and 47 Vict., c. 52, Sec. 55(7) (1883); 4 and 5 Geo. V, c. 59, Sec. 54(8) (1914)]. The language of Section 77B and of the provisions of the English Acts is almost identical,[1]

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phrasing was wholly inapplicable to pending bankruptcy or equity receivership proceedings."

But it was, of course, not necessary to eliminate the proviso clause in order to make it clear that a claim based on a covenant for damages or indemnity should be allowable, for such a covenant clearly is not terminated by reentry. Indeed, reentry is generally a condition precedent to the effective operation of such a covenant *Cf. Manhattan Properties, Inc.* v. *Irving Trust Co., supra; William Filene's Sons Co.* v. *Weed,* 245 U. S. 597. Secondly, making the provision expressly retroactive, rather than dispensing with the necessity of retaining the proviso clause, made its retention even more necessary if the intention was to bar a claim such as that in the instant case.

[1] Landlords' claims were first made provable by the English Bankruptcy Act of 1869. See *Manhattan Properties* case, *supra,* at page 332. The provision in that act was as follows:

> "Any person injured by the operation of this section [by a disclaimer, the English equivalent of a rejection] shall be deemed a creditor of the bankrupt to the extent of such injury, and may accordingly prove the same as a debt under the bankruptcy."

The provision in the English Act of 1883 and in the English Act of 1914 reads substantially the same.

except that the first English Act was not applicable to a rejection prior to its enactment.

The English courts have held that a landlord is "injured" by a disclaimer [rejection] if the fair rental value of the premises at the time the landlord repossesses them is less than the rent reserved in the lease, even in the absence of a covenant of indemnity or other special covenant for liability surviving termination of the lease, although under the English law the landlord could not recover damages in a lump sum against a solvent tenant; and that, accordingly, he has a claim provable in the bankruptcy proceeding to the extent of such difference. Not only is the provability of the claim not defeated by reletting by the landlord after the disclaimer, but the reletting is contemplated and the rent payable upon reletting is accepted as evidence of the fair rental value of the premises in the computation of the amount of the claim. *Ex Parte Blake*, 11 Ch. Div. 572; *Ex Parte Llynvi Coal & Iron Co., In re Hide*, L. R. 7 Ch. App. 28; *Ex Parte Leather Sellers Co.*, 3 Morrell 126 (Q. B. D. 1886); *Ex Parte Corbett*, 14 Ch. Div. 122 [1880]; *Ex Parte Walton*, 17 Ch. Div. 746 [1881]; *In re Hyams*, 93 L. J. Ch. 184 [C. A. 1923]; *Hardy* v. *Fothergill*, L. R. 13 App. Cas. 351 (House of Lords, 1888); *In re Carruthers*, 15 Reports 317, 2 Manson 172 (1895).[1]

[1] In an attempt to distinguish the English precedents the trustee in its brief in opposition to the granting of a writ (p. 10) relied on the provision in the English Act of 1869 (Sec. 23) that a disclaimed lease should "be deemed to have been surrendered" on the date of the order of adjudication, and in the English Act of 1883 [Sec 55(2)] and Act of 1914 [Sec. 54(2)] that disclaimer shall operate to determine the interest of the bankrupt as well as the trustee. The absence of these provisions in Section 77B, however, does not signify that termination of the lease under the state law after rejection has the effect of defeating the claim. If the claim is allowable, termination after rejection is

Under the test laid down in the instant case by the Court of Appeals (which, so far as can be determined from the language of its opinion makes no distinction between rejection before the statute and rejection after the statute) the claim is not allowable under Section 77B unless "under the applicable state law, it is capable of proof on the merits" (R. 72).[1] If this test should be applied literally, no landlord's claim would be provable under Section 77B, for neither the common law nor statute law of any state confers on the landlord a right of action against the tenant for *damages* in a lump sum for the loss which the landlord might suffer over the entire balance of

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contemplated even in the absence of an express provision providing that rejection shall terminate the interest of the bankrupt. A final decree in a proceeding under Section 77B releases the tenant from liability for future rent, so that the rejection plus the final decree has the effect of terminating the lease under that statute. Thus, the express provision in the English acts that adjudication or rejection shall terminate the lease, would, if contained in Section 77B, be material only in the event that proceedings were subsequently dismissed before final decree.

[1] In other places in its opinion the Court of Appeals reiterated the same thought in other language: "Section 77B makes such a claim provable provided there is evidence in support of it which constitutes proof as a matter of law" (R. 73). And again (R. 73-4): "It was necessary for the appellant to prove recoverable damages as a result of the rejection." "It therefore has no claim susceptible of proof as a matter of law" (R. 74). As the Court of Appeals expressed it in its opinion in these proceedings on the appeal of *Otis Estate Land Trust*, 83 F. (2d) 202, 206:

> "* * * It is necessary to have a claim against a debtor which the substantive law of landlord and tenant recognizes as an enforceable claim in order to have a provable claim under Section 77B. That section does not extend the liability of a lessee beyond what it otherwise would be under applicable law. *If under such law a landlord would have a claim against a lessee for damages or indemnity under a covenant contained in a lease which would have been recoverable in a civil action had there been no 77B petition approved, such claim may be proved* in the 77B proceedings and allowed to the limited extent above indicated."

the term. Apparently the Court of Appeals did not intend this test to be taken literally, for in its subsequent decision in *In re United Cigar Stores Co. (Kuehner and Fischer, Appellants)*, 85 F. (2d) 35, it held provable a claim of a landlord under a rejected lease which contained a covenant obligating the tenant to indemnify the landlord against loss of rent.

Clearly the "rejection" provision of Section 77B was not intended to be limited to claims based on leases which contain covenants for liquidated damages or indemnity. For, the reference in the limitation provision immediately following the rejection provision (see *supra*, p. 4) to a "claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate *or* for damages *or* indemnity under a covenant contained in such lease", shows conclusively that a claim "for injury resulting from the rejection" does not depend upon the presence of a special covenant in the lease.

This was recognized subsequently by the Court of Appeals in its decision in *In re Paramount Publix Corp. (Madison-Toledo Co.* v. *Paramount Pictures, Inc.)*, *supra*, in which it held provable a claim based on a rejected lease without a covenant for damages or indemnity (which had not been terminated prior to the enactment of the statute). It is implicit from the decision of the court, though it was not discussed, that termination of the lease before the confirmation of the plan would not defeat the claim.

In some respects this is even clearer under Section 77B than under the provisions of the English Acts:

**(1) The claim is "limited" with reference to the date of termination of the lease:** The limitation provision

immediately following the "rejection" provision provides:

> "The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity * * *, but shall be limited to an amount not to exceed the rent * * * for the three years next succeeding *the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition,* plus unpaid rent accrued up to such date of surrender or reentry: * * *."

Thus the parity portion of the claim for injury resulting from the rejection is measured with reference to surrender of the premises to the landlord *or* reentry by the landlord. While "surrender" as here used apparently does not refer to a technical surrender of the leasehold estate, reentry (the date of which is controlling when reentry by the landlord precedes surrender) is a technical term denoting an act which puts an end to the leasehold estate. That Congress intended the word "reentry" to have its ordinary meaning is shown by its failure to use the expression "repossession of the premises by the landlord" in juxtaposition to "surrender of the premises to the landlord".

**(2) The landlord's claim being for damages and not for future rent, the statute contemplates termination of the lease after rejection:** Whatever else the limitation provision may mean, the legislative intention is clear that the claim shall not be allowed in an amount in excess of the total loss which it is estimated the landlord will suffer, where such total loss is less than the amount of three years' rent. No way of es-

timating the landlord's loss over the remainder of the term has ever been suggested other than the difference between rent reserved, discounted, and the fair rental value of the premises for the remainder of the term.[1] Allowability thus contemplates subtraction of the fair rental value of the premises in calculating damages. *Crediting the rental value of the premises contemplates use of the premises by the landlord for the purpose of reletting.* Occupation of the premises by the landlord; or reletting (in many states), after the tenant's abandonment, effects a termination of the liability of the tenant under the rent covenant.[2] It is apparent, therefore, that provability of a landlord's claim presupposes repossession by the landlord and occupation of the premises by the landlord or reletting, without regard to whether the landlord's acts had the effect of terminating the tenant's liability on the rent covenant under the applicable state law of landlord and tenant.

**(3) If allowability were conditioned on failure to terminate, the claim would have to be reserved; but present allowance is expressly contemplated by the statute:** In the District Court the respondent Preferred Stockholders' Protective Committee argued that the statute provides that termination of the tenant's liability on the lease at any time prior to confirmation of the plan would bar the landlord's claim. Logically, if termination of the tenant's liability on the lease at any time after rejection has any materiality, the

[1] See the petitioners' brief in *Kuehner and Fischer* v. *Murphy* (No. 354), page 12.

[2] Certainly there is nothing to indicate that Congress intended to distinguish between a landlord who, upon repossession after rejection, occupies the premises himself, and one who thereupon relets.

claim could not be allowed at all, because of the possibility of the termination of the tenant's liability at some time prior to the expiration of the term. The claim in that event would have to be reserved as a charge against the assets of the company, and the landlord would not be entitled to vote upon the plan, since only the owners of *allowed* claims are entitled to vote upon the acceptance of a plan (subdivision (e) (1), Section 77B[1]). Yet this would be in the teeth of the rejection provision, which provides that "any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its *acceptance* and confirmation, be deemed to be a creditor". This clearly evidences an intention that the landlord's claim shall be allowed before any plan is confirmed.

Thus under the Bankruptcy Act prior to its amendment, provability was denied by Congress because the state law of landlord and tenant made the claim too contingent. In enacting Section 77B and amending Section 63(a), Congress obviously intended to change the rule of the *Manhattan Properties* case, to provide that the technical law of landlord and tenant of the states should not be applied in the administration of the federal bankruptcy law, and that instead, for the purpose of administration of the bankruptcy law, leases should be placed upon the same footing as executory contracts relating to personalty. Rejection of the lease, for the purpose of administration of the act (whatever the effect may be under the applicable

[1] Subdivision (e) (1) provides:

> "A plan of reorganization shall not be confirmed until after it has been accepted * * *, and such acceptance shall have been filed in the proceeding by or on behalf of creditors holding two-thirds in amount of the claims in each class whose claims have been *allowed*. * * *"

state law in the event that the proceedings ultimately should be discontinued without a reorganization being effected), effects an anticipatory breach and termination of the lease, and termination under the state law thereafter is immaterial so far as the operation of the statute is concerned. See Keegan, Rights of Landlord and His Bankrupt Tenant, 21 A. B. A. J. 379, 383; 2 Univ. of Chic. L. Rev. 629.

(c) *Rejection Prior to Section 77B.*

The Court of Appeals itself recognized in its decisions in the *Paramount Publix* case and on the appeal of *Kuehner and Fischer, supra,* that the rejection provision is applicable to rejection prior to the enactment of the statute. See also subdivisions (a) and (p), *supra,* at page 3. The issue, thus, is simply as to the meaning of the provision, not as to its applicability to the case at bar.

The same phraseology in the same sentence of the statute covers both rejection before enactment of the statute and rejection after its enactment, without any restrictive qualification as to prior rejection:

> "*In case an* executory contract or *unexpired lease of real estate* shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or *shall have been rejected by a trustee* or receiver *in bankruptcy* or receiver in equity, *in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall,* for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor."

Therefore, Congress must have intended the statute to have the same operation and effect in both cases.

As this Court said in *Moore Ice Cream Co.* v. *Rose*, 289 U. S. 373, 378:

> "There is a unity of verbal structure that is a symptom of an inner unity, a unity of plan and function. The field of operation is not shifted between the clauses of a sentence."

As we have seen, reentry, and occupation of the premises by the landlord or reletting, after rejection in a proceeding under Section 77B, not only do not bar the claim, whether or not the effect of the landlord's acts is to terminate the tenant's liability under the applicable state law, but are actually contemplated by the statute. Similarly in the case at bar the restoration of the premises and reletting by the landlord after rejection by the trustee in bankruptcy in the prior bankruptcy proceeding do not defeat the claim, whether or not the landlord's acts effected a surrender of the lease by operation of law under the law of New Jersey.[1]

In its opinion on the appeal of *Kuehner and Fischer, supra,* the Court of Appeals said that it is not necessary to read the rejection provision as having the effect of making over the contract of the parties "by imposing a liability for future rent on the lessee after the term had ended" (at p. 37).[2]

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[1] The argument in this brief—that termination after rejection is immaterial—is intended to be restricted to the facts of the instant case, to wit, to a termination resulting from restoring and reletting the premises. The termination in the instant case did not result from an *express release* of a tenant from all obligations under the lease in return for a consideration, or from an *assignment agreement* providing for the acceptance of a surrender in return for an express consideration.

[2] But the rejection provision does not impose "a liability *for future rent* on the lessee after the term has ended". It merely recognizes a claim for *damages* after the term is ended because of the tenant's previous bankruptcy.

The Court said further:

> "It is enough if the language be taken to mean that the 'rejection' of a lease shall be a present breach of all the lessee's promises, either to pay rent, to rebuild, to cover taxes or whatever else they may be. *Indeed, if it continues his liability after reentry, it was redundant to include covenants 'for damages or indemnity'.*"

The first sentence of this quotation would seem to require a conclusion that it was the intention to make a claim based on rejection allowable, irrespective of termination thereafter. The second sentence, which appears to state the court's reason for retreating from this conclusion, is fallacious, for it assumes that the limitation provision, from which the words "for damages or indemnity" were quoted, made claims allowable. In fact, the inclusion of those words in the limitation provision following the rejection provision was simply to make clear that a claim based on a lease containing a covenant "for damages or indemnity" was to be "limited" as well as a claim "for injury resulting from the rejection".[1]

The rejection provision, as applied to a rejection prior to the statute, cannot be restricted to leases containing special covenants any more reasonably than when applied to a rejection in a proceeding under Section 77B, which, as we have seen, is not tenable (see *supra*, p. 17). In a subsequent decision, already

[1] Claims under covenants for damages or indemnity (whether or not the lease was rejected before termination) would have been provable under the broad definition of creditors already set forth in subdivision (b) (10), which includes holders of claims under executory contracts, *whether or not such claims would otherwise be provable.* But for the inclusion in the limitation provision of a claim "for damages or indemnity", as well as a claim for injury resulting from rejection, the former might not have been limited.

referred to, the Court of Appeals recognized this and expanded its conception of the meaning of the rejection provision as applied to a rejection prior to the enactment of the statute to include a claim based on a rejected lease without special covenants which had been kept alive after rejection. *In re Paramount Publix Corp.* (*Madison-Toledo Co.* v. *Paramount Pictures, Inc.*), *supra.* In that case at the date of the original bankruptcy the premises had been entirely sublet and the landlord did nothing after rejection by the trustee in bankruptcy except to collect rents from the sub-tenant then in possession. Thus, under the doctrine of the *Paramount Publix* decision, the petitioner's claim in the case at bar would have been allowable if the landlord had merely continued to collect rent from the sub-tenants in possession.[1]

Certainly, Congress did not intend the allowability of landlords' claims to be dependent upon such technicalities of state law. Indeed its object in including the rejection provision in Section 77B and in Section 63(a) was to end the necessity of dealing with the

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[1] One sentence in the opinion of the Court of Appeals in the *Paramount Publix* case evidences the inconsistency between its decision in the case at bar and its view of the effect of the rejection in the prior bankruptcy proceeding (p. 86):

> "*As the lease was not terminated under the Ohio law until it was rejected* by the debtor's trustees, the claim should have been allowed for the rent and taxes due on the date of the rejection and for injury, if proved, due to the rejection."

If the rejection in the prior bankruptcy proceeding terminated the lease *for the purpose of the application of Section 77B*, then any subsequent termination under the state law [at least any resulting from surrender by operation of law] after such rejection [and termination] ought to be utterly immaterial.

In an opinion in these proceedings on the claim of *Evelyn Picker and Myrtle Picker*, not reported (decided March 16, 1936), District Judge Coxe also refers to rejection by the trustee in bankruptcy of this debtor as having terminated the subleases previously made by the debtor.

quaintly spelled maxims of Lord Coke. Nor does the construction of the Court of Appeals conform to the familiar direction that a remedial statute, which Section 77B obviously is, should be interpreted liberally and reasonably and in accordance with the fair import of its terms. *City of Chelsea* v. *Dolan*, 24 F. (2d) 522; *Emerson* v. *Castor*, 236 Fed. 29, 33.

(d) *If the Construction of the Court of Appeals be Adopted, the Rejection Provision, as Applied to Prior Rejection, Is Rendered Practically Meaningless. Moreover, Grossly Inequitable Results Would Follow.*

**(1) The narrow construction of the Court of Appeals practically nullifies the rejection provision as applied to a rejection prior to the enactment of the statute:**

(a) *Number of landlords benefited:* The only landlord who, as a practical matter, might be benefited by the rejection provision under the doctrine of the Court of Appeals is the one who was fortunate enough to have had the premises entirely sublet by the tenant at the time of bankruptcy (*Paramount Publix* case). Such a landlord was in a position to reap income from his property without terminating the lease by collecting rent from the subtenants so long as they remained in possession. Where the premises were not sublet, the landlord in order to realize value from his property was compelled to reenter and occupy himself or relet. Obviously, no landlord would have allowed the premises to remain idle in the hope of collecting the full rent against an undischarged corporate bankrupt. Yet the landlord's occupation or reletting generally had

the effect of terminating the lease,[1] although both as a practical matter merely had the effect of mitigating the landlord's damages. Thus, if Congress had any intention of benefiting landlords whose leases had been rejected prior to the enactment of the statute, it must be deemed to have intended to benefit the great majority of that class of landlords and not the paltry few who were not compelled to terminate. Otherwise provability would depend upon fortuitous circumstances—such as the state in which the premises were located, or whether the premises had been sublet, or whether the premises had been occupied by the landlord instead of relet, or whether the premises had been substantially altered by the tenant before abandonment.

The natural common sense meaning of "injury resulting *from the rejection*" means the injury which the landlord suffered as a result of the release of the assets in the bankrupt estate from liability for rent under the lease. The liability of the corporate *debtor* which survived rejection, whatever may have been its value, would be terminated, in any event, by the final decree in these proceedings. Its termination before final decree, but after rejection, therefore, was naturally deemed of no significance by Congress.

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[1] In no state could the landlord occupy the premises himself without terminating the lease, and even in those states in which he ordinarily could relet without terminating the lease (see *infra*, p. 45), he could not, where the condition of the property made it impossible to relet without changing the alterations made by the tenant and restoring the premises to their original condition, for under the doctrine of the Court of Appeals such restoration itself would terminate the lease.

For instance, in the case at bar the landlord could not have relet without restoring the wall between the two buildings and she could not restore without, as the Court of Appeals held, effecting a surrender. Thus she would have had to allow the premises to remain idle from November, 1932, in order to preserve her claim.

(b) *Amount of damages*: Under the construction adopted below, the landlord must, in order to have retained his claim, have allowed the premises to remain unoccupied after rejection, and at least up to the date of institution of proceedings under Section 77B. Two or three years may have elapsed after rejection by the trustee in bankruptcy before the enactment of Section 77B and the institution of a proceeding thereunder. Yet, under the measurement of damages which the Court of Appeals itself has laid down (appeal of *Kuehner and Fischer, supra*), the landlord's claim for such two or three year period could not exceed the difference between the rent reserved and the fair rental value of the premises for such period. If the premises were relet without loss for the remainder of the term after the institution of proceedings under Section 77B, or if the lease expired at that time, *the construction adopted by the Court of Appeals would result in the allowance of a claim for less than three years' rent and less than the loss actually suffered by the landlord.* Congress intended no such unjust result.[1]

**(2) The claim is "limited" with reference to termination of the lease prior to enactment of the statute:** The amount of the parity portion of a landlord's claim for injury resulting from rejection is expressly measured with reference to the "date of surrender of the premises to the landlord or the date of reentry of the land-

[1] Yet the only alternative would be to apply a different measure of damages to claims based on rejection prior to the statute so that in the case of such claims the measure of damages would be the full amount of the rent reserved for the period intervening between the date of the rejection by the trustee in bankruptcy and the date of institution of proceedings under Section 77B (although the premises could have been relet for 100% of the rent originally reserved in the lease, or more). Such a rule would be unjust to other creditors.

lord, whichever first occurs, whether *before* or after the filing of the *petition*". Reentry, as we have seen, means a technical reentry terminating the tenant's liability. It could not have been intended to limit this provision to termination of liability on the lease *after* the enactment of *the statute* but *before* the filing of *the petition* thereunder, for the statute clearly contemplated that a petition might be filed immediately upon its enactment (*i. e.*, its effective date). Hence, the statute must have contemplated the landlord's termination of the tenant's liability on the lease by reentry before the enactment of the statute (but after rejection in the prior bankruptcy proceeding).[1]

**(3) If restricted to a lease which has been kept alive, the rejection provision is rendered superfluous as to prior rejections:** A lease which was kept alive after rejection would have remained vested in the bankrupt tenant (*In re Frazin, et al.*, 183 Fed. 28), and consequently, upon the filing of a petition under Section 77B would have fallen into the reorganization estate. In such event the debtor or the reorganization trustee would have had to reject the lease again, if burdensome. Consequently, any landlord's claim could in such event be based upon the provision which relates to rejection "pursuant to direction of the judge given in a proceeding instituted under" Section 77B, and the reference to *rejection in a prior proceeding* would be redundant.

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[1] Of course, the lease must not have terminated prior to the institution of the original bankruptcy proceeding, for in that event the trustee would have had nothing to reject. It is for this reason, no doubt, that the amendment to Section 63(a) does not, as does Section 77B, measure the amount in which the claim may be allowed with reference to surrender or reentry of the premises "*before or after the filing of the petition.*"

**(4) The construction of the Court of Appeals would bar a claim under Section 77B, though provable in a prior bankruptcy proceeding:** In an ordinary bankruptcy proceeding where Section 63(a), as amended, is applicable, the landlord would have a provable claim to the extent of at least one year's rent. If after his claim has been allowed the landlord should reenter and terminate the lease and the bankrupt should then file a petition under Section 77B, under the doctrine laid down by the Court of Appeals in the case at bar, the landlord would have no provable claim under Section 77B at all; for, at the date of the institution of the proceeding under Section 77B the tenant would be under no liability to the landlord under the applicable state law because of the prior termination. There is certainly nothing to indicate that Congress intended that the landlord in the latter case should lose his claim.[1]

Yet it is obvious that the language relating to rejection in a proceeding pending "prior to the institution of a proceeding under" Section 77B, cannot cover the landlord's claim in the case supposed without also covering the landlord's claim in the case at bar, since, as we have already shown, the rejection provision of the statute applies, in identical language, to rejections prior to the enactment of the statute as well as to rejections after its enactment.[2] The provision

[1] On the contrary, Congress clearly intended that, if the bankruptcy liquidation proceedings should be converted into reorganization proceedings (in which shareholders might participate), the landlord's claim should be increased, to an amount equal to three years' rent (so far as other creditors are concerned) and to the full amount of his claim (so far as stockholders are concerned).

[2] Moreover, Congress no doubt realized that the conversion of a bankruptcy liquidation proceeding into a reorganization proceeding under Section 77B would, no doubt, be very infrequent in the future, since corporations ordinarily would avail themselves of Section 77B before resorting to liquidation.

obviously was intended to have the same effect in both cases and to allow the landlord to establish a claim for the injury which was inflicted on him by the refusal of the trustee in bankruptcy to assume the lease as an obligation of the estate.

(e) *The Statute Does Not "Create" a Substantive Right.*

The only argument that has been made against the construction for which the petitioner contends is that Congress did not intend to create a legal claim[1] or substantive right where none theretofore existed at common law or in equity. But the statute, if construed as contended for, does not create a substantive right where none previously existed [either where the lease was terminated prior to the enactment of the statute, but after rejection in the prior bankruptcy proceeding; or where the lease is terminated after the statute (and after rejection in a bankruptcy or equity proceeding instituted after the enactment of the statute) but before the institution of proceedings under Section 77B]. *In both cases the leases were in existence at the time of the institution of the original bankruptcy or equity proceeding.*

Properly viewed, therefore, *the question in the case at bar is not whether Congress intended to create a right where none existed theretofore, but whether it intended that a new division of "the pot" should be made* among the creditors of a tenant whose assets

[1] The Special Master (R. 39) so phrased his argument. The statute obviously did create *claims* where none theretofore existed, for it created a claim for *damages* unknown to the common law. What the Master means is that the statute did not create any *substantive rights* against a debtor where none existed prior to the enactment of the statute.

were still being administered by the bankruptcy court at the time the purpose of the bankruptcy proceeding was converted from liquidation to reorganization pursuant to the statute, including among such creditors all those who had valid leases in existence at the time of institution of the proceeding. It is clear that Congress did intend to change the rule of the *Manhattan Properties* case and thus to provide for such a new division of the pot, both in proceedings instituted after the enactment of the Act of June 7, 1934, and also in bankruptcy proceedings pending at the date of its enactment:

> (1) where the time for filing claims had not expired,[1] or
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> (2) where, whether or not the time for filing claims in the bankruptcy proceeding had expired,[2] a petition for reorganization under Sec-

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[1] The Act of June 18, 1934, 48 Stat. 991, further amended Section 63(a), as amended by the Act of June 7, 1934, to provide "that the provisions of this clause (7) shall apply to estates pending at the time of the enactment of this amendatory Act *in which the time for filing such claims has not expired.*" The evident purpose of this amendment was to avoid the confusion and disorganization which would have resulted if the time for filing claims had to be reopened and a redivision of the bankrupt estate made.

[2] The District Court was obviously wrong in thinking (R. 50-1) that the rejection provision in Section 77B was applicable only if the petition under Section 77B was filed prior to the expiration of the period for filing claims in the prior bankruptcy proceeding. The Act of June 18, 1934, amended only Section 63(a), not Section 77B. Subdivision (c)(6) of Section 77B expressly directs the reopening of the time for filing claims, whether or not the time for filing claims in the prior bankruptcy proceeding has expired. The district court's conception as to the relevancy of the time for filing claims in the prior bankruptcy proceeding was rejected by the Court of Appeals in its decisions in the *Paramount Publix* case, *supra*, and on the appeal of *Kuehner and Fischer* in these proceedings, *supra*.

tion 77B should be filed in such bankruptcy proceeding and approved by the court.[1]

The language and scheme of the statute seem to us so clear and unambiguous as to compel this conclusion without the necessity of examining the legislative history of the statute or the conditions which existed at the time of the enactment of the statute (*Helvering* v. *City Bank Farmers Trust Company*, 296 U. S. 85, 89). As we have seen, however, reference to the legislative history of the statute and the contemporaneous conditions existing at the time of the enactment of the statute confirm the plain meaning of the language used, and the unreasonable results which would be effected by the adoption of the narrow construction of the Court of Appeals are strongly persuasive reasons against it.

If Congress intended the statute to mean something other than what the language used plainly means, it would have retained the original proviso clause in the House bill, which would have barred the claim of any landlord who terminated his lease before the enactment of the statute or any time after the enactment of the statute up to the time of the allowance of the claim in the proceeding under Section 77B; or, at least it would have inserted a less stringent qualification, such as "provided that the lease has not or shall not have been terminated prior to the institution of proceedings under this Act". The absence of any qualification in the language used and the elimination of the qualification initially used, we submit, compels the

[1] In *In re Paramount Publix Corporation, Greenberg* v. *Paramount Pictures, Inc.*, 85 F. (2d) 42, 44, the court below said of a situation like that in the case at bar:

> "* * * reorganization becomes an amplification or new end product of the original bankruptcy, just as though the bankrupt * * * had proposed a composition. * * *"

conclusion, particularly in view of the remedial purpose of the statute, that termination by surrender or reentry before the enactment of the statute does not bar the claim under Section 77B.

*The construction adopted by the Court of Appeals ignores every one of the extraordinary consequences which flow therefrom, and its decision, we submit, is equivalent to judicial legislation.*

## POINT II.

**There are no doubts as to the constitutionality of the statute which can influence its interpretation.**

(a) *The language of the statute is clear and unambiguous.*

The trustee urges that the plain language of the statute should not be followed in the case at bar because that would give it a retroactive effect which would "create" a claim where none existed before and would deprive the debtor of a vested defense which it theretofore had to any cause of action which might have been brought against it on the lease.

It has not been suggested that there is any doubt as to the constitutionality of the statute in its prospective operation,—*i. e.*, as applied to leases which were subsisting obligations at the date of enactment, irrespective of whether they were rejected before or after the enactment of the statute, and irrespective of whether or not the debtor corporation may have been relieved of all liability prior to the institution of proceedings for reorganization.

Nor, apparently, is it urged that the language of the rejection provision permits it to be given a

different meaning as applied retroactively to the petitioner's claim from the meaning which clearly must be given to it in its prospective operation. The trustee's argument appears to be merely that the statute cannot be applied to the claim in the case at bar because its retroactive operation in this case would raise doubts as to its constitutionality.

It is true that doubts as to constitutionality may influence the *interpretation* of a statute, but the Court of Appeals did not suggest any permissible interpretation of the language of the statute which would exclude the petitioner's claim. In fact, the Court did not even attempt to interpret the statute, but only refused to *apply* it to the petitioner's claim because of doubts as to its constitutionality. In so holding, the Court of Appeals has, in effect, invalidated and stricken down the statute as applied to this case, which was beyond its power, since no direct attack had been made on its constitutionality.

The only suggestion made by the Court of Appeals which can in any sense be deemed to be an interpretation of the rejection provision is its statement in its opinion on the appeal in these proceedings of *Otis Estate Land Trust,* 83 F. (2d) 202, 206, where it said:

> "But there is no new definition of a claim; only of a creditor."

Obviously, however, if a landlord is deemed to be a *creditor,* he must be deemed to have a *claim* entitled to participate in the reorganization. Otherwise the rejection provision is entirely meaningless. For, if the doctrine of the Court of Appeals (that there must be a lease in existence at the time of the enactment of the statute) is correct, the definition of creditors and claims in subdivision (b)(10) would

have been sufficient to make every landlord's claim allowable which in its view would be allowable under the rejection provision. But the rejection provision is not meaningless either in its retrospective or prospective application. By including the provision as to prior rejections, Congress obviously intended to permit landlords like the petitioner to participate in a reorganization and, while so doing, it also included language covering rejections in the future in order to make it clear beyond doubt that claims based on leases without special covenants should be allowable.

As we have shown, (1) the statute is expressly applicable to prior rejections (*supra*, p. 21); (2) Congress did not intend to exclude the landlord whose lease did not contain a special covenant for damages or indemnity (*supra*, pp. 17, 24); and (3) it eliminated from the House bill the *proviso* which had excluded the landlord whose lease had been or should be terminated after rejection and inserted in place thereof a provision which measured a part of his claim with reference to the date of his reentry, whether *before* or after the enactment of the statute (*supra*, pp. 13, 32). In short, the meaning of the statute is so clear that doubts as to its constitutionality as retroactively applied cannot influence its interpretation. Such doubts, however grave they may be, will not authorize the courts to adopt an interpretation which is patently at variance both with its express terms and with its plain intent.

As this Court said in *Moore Ice Cream Co.* v. *Rose*, *supra*, at page 379:

> "But avoidance of a difficulty will not be pressed to the point of disingenuous evasion. Here the intention of the Congress is revealed too

distinctly to permit us to ignore it because of mere misgivings as to power."

(b) *No question as to the constitutionality of the statute has been raised in the case at bar; none of the respondents was in a position to question its constitutionality.*

Neither the trustee nor any other respondent has at any time directly questioned the constitutionality of the statute if it be interpreted as permitting the allowance of the petitioner's claim. Its constitutionality cannot be attacked for the first time in this Court.

Moreover, none of the respondents was in a position to attack directly the constitutionality of the statute for certain reasons which, we submit, also make unavailable to them the argument of constitutional doubts in aid of statutory interpretation, by which they seek indirectly to inject the question of constitutionality into this case.

The trustee has no independent standing to question the constitutionality of the statute. Its right in that respect cannot rise higher than the rights of those whom it represents; (1) the debtor and its stockholders, and (2) other creditors. Neither creditors nor stockholders are in a position in this case to attack the constitutionality of the provision which the statute has made for this petitioner.

(1) *As to creditors.*

The only injury of which creditors of the debtor whose claims were allowed in the prior bankruptcy proceeding before Section 77B was enacted can complain is that the treatment of part of the claim of the petitioner and those similarly situated on a parity with their claims would dilute their participation in the

reorganization. Consequently, the only provision of the statute the constitutionality of which they or the trustee on their behalf could have attacked is the limitation provision requiring landlords' claims to be treated on a *parity* with other claims to the extent of three years' rent.

But the parity provision is clearly severable. Even if it had been directly attacked and invalidated, that would not have stricken down the rejection provision on which depends the general allowability of the petitioner's claim. Therefore, even if doubts as to the constitutionality of the parity provision could affect *its* interpretation, they cannot affect the interpretation of the *rejection* provision.

However, it cannot be urged that the parity provision should be construed so as to deny landlords' claims partial parity with other creditors, for its language is indisputably plain and unambiguous in this respect and can have no meaning other than that claims which are made allowable by the rejection provision (claims "for injury resulting from the rejection") shall be treated on a parity with other claims to a limited extent.

In any event, there is no serious doubt as to the power of Congress to accord to the petitioner's claim a ranking on a parity with claims already established in the bankruptcy proceeding. While under the state law creditors had a right to enforcement of their respective claims in priority to the interests of stockholders, they obviously had no right under that law, nor under the terms of their contracts, to enforcement of their claims in priority to landlords, to whom their debtor was also legally obligated. Nor may the provisions of the Bankruptcy Act as they existed at the time of the extension of credit be read into the contracts of the creditors, for Congress "may amend or repeal [the Bankruptcy Act] at

pleasure, provided it does not disregard the requirement of uniformity." *City of Chelsea* v. *Dolan,* 24 F. (2d) 522, 523. Creditors had no vested interest in the then provisions of the Bankruptcy Act, even after the filing of their debtor's petition in bankruptcy. Congress could change the then existing bankruptcy system, even after the filing of the petition. *City of Chelsea* v. *Dolan, supra.*

(2) *As to the debtor and its stockholders.*

The statute does not have the effect of destroying the vested defense which the debtor would have under the applicable state law in the event that the reorganization proceedings should be dismissed. The statute merely changed the statutory rule of non-provability and provided that termination of the lease should not deprive those who had valid leases at the time of the original bankruptcy from participating in the debtor's reorganization. Neither the debtor nor its stockholders may complain of that.

The debtor corporation voluntarily filed its petition for reorganization under Section 77B. The debtor cannot avail itself of the benefits of the statute and at the same time seek to escape its burdens. *Great Falls Mfg. Co.* v. *Attorney General,* 124 U. S. 581; *Wall* v. *Parrot Silver & Copper Co.,* 244 U. S. 407; *St. Louis Casting Co.* v. *Prendergast Const. Co.,* 260 U. S. 469. The stockholders of the debtor by acquiescing in the debtor's seeking relief under Section 77B have similarly estopped themselves.

Congress might have restricted the benefits of the statute to going corporations not already in bankruptcy. It was a matter of grace to extend its benefits to corporations which already had been adjudicated bankrupt. It was reasonable for Congress to provide that, if a corporation which had already been adjudi-

cated bankrupt desired to effect a reorganization under the provisions of the new statute, all persons to whom it was legally obligated at the time it originally went into bankruptcy should be permitted to participate in such reorganization, and particularly all persons who suffered injury as the result of the bankruptcy.

Whether or not these considerations are equally applicable to the case of a debtor which has involuntarily been subjected to the provisions of Section 77B, it is clear that doubt as to the constitutionality of the rejection provision in a case where an involuntary petition has been filed under Section 77B cannot affect its construction in the case of a voluntary petition as in the case at bar. Even if unconstitutional in an involuntary case, there is nothing to indicate that Congress did not intend that the provision should be applicable in a voluntary case. If in a case involving an involuntary proceeding, the provision should be held unconstitutional (as applied to leases terminated before the enactment of the statute) there would result merely a functional severance of the rejection provision and its restriction to voluntary proceedings. *Cf. Loeb* v. *Columbia Township Trustees,* 179 U. S. 472, 490; *People* v. *Knapp,* 230 N. Y. 48, 60.

(c) *Even if the debtor or its stockholders could have attacked the constitutionality of the statute, general principles of constitutional law would support its validity.*

The power of Congress over the "subject of bankruptcies" extends to whatever is necessary or *reasonably adapted* "under modern conditions to deal adequately with the relationship existing between embarrassed debtors and their creditors". *Campbell* v. *Al-*

*leghany Corp.*, 75 F. (2d) 947, 955, cer. den. 296 U. S. 581; *In re Reiman*, 20 Fed. Cas. 490, 496; see also, *Hanover National Bank* v. *Moyses*, 186 U. S. 181; *In the Matter of Edward Klein*, 42 U. S. 277; *Continental Bank* v. *Rock Island Ry.*, 294 U. S. 648, 670; *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, 582, *et seq.*

It is within the bankruptcy power to provide for the provability or nonprovability of claims. *Manhattan Properties, Inc.* v. *Irving Trust Co., supra.*[1] Provision for provability is merely incidental to an equitable distribution of a debtor's property among his creditors *as of the date of the institution of the bankruptcy proceeding*, which is one of the ends of a bankruptcy law. *Kothe* v. *R. C. Taylor Trust, supra*, at page 227, and cases cited in *Louisville Bank* v. *Radford, supra*, at page 507.

Even if after the petition was filed in the case at bar and before the claim was made provable, the debtor's *individual liability* on the lease had been terminated under the applicable state law, that would not have insulated the *bankrupt estate* from the exercise by Congress of its power to provide for the provability of the claims of all persons to whom the bankrupt was legally obligated at the time of bankruptcy.

The plenary power of Congress to legislate on the subject of bankruptcies is sufficient to widen the class of persons entitled to participate in the reorganization of an estate already in bankruptcy, even if the provision for participation disregards *vested defenses*

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[1] This Court said (at p. 332), "The issue is not one of power, for plainly Congress may permit such claims or exclude them."

accrued prior to its enactment. *Cf. Norman* v. *B. & O. R. Co.*, 294 U. S. 240, and cases cited therein.[1] The bonds involved in *United States* v. *Bankers Trust Co.* (reported *sub nom. Norman* v. *B. & O. R. Co.*, 294 U. S. at p. 294) had become payable prior to the enactment of the resolution striking down "gold clauses", and the cause of action thereon had vested. There is obviously no difference between a *vested cause of action* arising out of a contract, such as there involved, and a *vested defense* arising out of the local law, such as involved in the case at bar.

The only limitation is that the provision enacted pursuant to the federal power shall bear a reasonable relation to an end connected with the object of the power. The provision for provability in Section 77B is not arbitrary, but does, as we have seen, bear a reasonable relation to a legitimate end,—viz., to achieve an equitable participation in the debtor's assets by those to whom the debtor was obligated as of the date of the original bankruptcy, where reorganization was sought by a corporation already in bankruptcy or by its creditors or stockholders.

Possibly Congress might constitutionally have excluded landlords whose leases had been terminated under the applicable state law. But it certainly is true that letting in those landlords is not only not arbitrary and unfair, but is the only equitable provision that Congress could have made, in recognition of the fact that their injury, which resulted from the bankruptcy proceeding, had been as real as the

[1] None of the cases cited by the trustee in its brief in opposition to the granting of a writ (p. 15) holding that a vested defense cannot be destroyed by subsequent legislative action involves a statute enacted under a federal power.

injury inflicted on other landlords whose leases had not been terminated.

In the case at bar the lease was a valid subsisting obligation of the debtor at the date it filed its voluntary petition in bankruptcy in 1932. In no proper sense, therefore, does the statute *create* a substantive right. The debtor and its stockholders, after filing the original voluntary petition in bankruptcy in 1932, had no interest in the assets of the debtor entitled to constitutional protection other than the right to any surplus of assets which might result after the payment in full of its creditors as of the time it originally availed itself of the bankruptcy process. The provision in question is not in the least analogous to a subsequently enacted provision (to which the trustee referred in its brief (p. 14) in opposition to the granting of a writ) providing that claims which are not valid at the time of the filing of the petition (such as those subject to the defenses of the statute of limitation, the statute of frauds, or the statute of usury) shall nevertheless be provable. Obviously the rejection provision applies only to *valid leases* subject to no defenses at the time of rejection by the trustee in the prior bankruptcy proceeding.

Section 77B, however, goes no further than to do away for the purpose of the bankruptcy law with the historical distinction between leases and other types of obligations, all of which were valid at the time of the institution of the original bankruptcy proceedings, and to provide, as a condition of the acceptance of the benefits of the reorganization statute in bankruptcy proceedings pending at the date of its enactment, that the rights and priorities of the creditors and stockholders should be adjusted

in accordance with their substantive rights as they existed at the time of the original bankruptcy.[1]

## POINT III.

**Under the law of New Jersey the liability of the debtor under the lease survived restoration and reletting of the premises.**

Even under the doctrine of the Court of Appeals, as enunciated in the *Paramount Publix* case (*supra*, p. 24), the petitioner's claim is allowable if at the time of the institution of proceedings under Section 77B the debtor was still liable on the lease under the law of New Jersey, the situs of the property.

The burden of proving facts establishing a surrender rests on the party alleging surrender. *O'Neil* v. *Pearse*, 87 N. J. L. 382, aff'd. 88 N. J. L. 733; *Liskovsky* v. *Blau*, 114 N. J. L. 324; *Shalet* v. *Klauder*, 34 F. (2d) 594. The only facts bearing on the question whether a surrender was effected which were established by the trustee (by including them in the two stipulations of fact which constitute the only evidence in the case [R. 19, 33]) are these:

The debtor upon its adjudication on August 28, 1932, abandoned the premises. The trustee in bankruptcy thereafter collected rents from the sub-tenants in possession, but on November 11, 1932, rejected the

[1] The claim made provable is for *damages* only, so that subsequent termination of the lease would have been contemplated if the statute had been enacted prior to the commencement of the original bankruptcy proceedings in 1932 (see *supra*, p. 18). The final decree will release the debtor and its assets from all liability for future rent, as would the state law if the proceedings were dismissed.

lease and abandoned the premises. After rejection of the lease, the landlord relet various portions of the premises to sub-tenants in possession and subsequently relet other portions of the premises to others. The lease contained no clause expressly authorizing the landlord upon the tenant's abandonment or default to relet for the tenant's account; nor, on the other hand, did it provide that the term of the lease should end upon the landlord's re-entry or re-possession after the tenant's abandonment or bankruptcy (R. 23).

The stipulations were silent as to whether the landlord in reletting intended to relet for the debtor's account or to accept a surrender.

As has been mentioned (*supra*, p. 3), though the stipulations were silent on the subject, the Master "found" that the landlord had filed in the bankruptcy proceeding "a claim for $1,980.99 for alleged expenditures in restoring a party wall and in closing up a common entrance in the demised premises". The Court of Appeals went further and "found" (R. 72) that the debtor before reletting "made structural changes in the premises to restore them to the condition they were in when leased by rebuilding a party wall and closing up a common entrance, all at an expense of $1,980.99." Although not established by the record and not drawn in issue by the trustee's objection to the claim (and although for that reason alone the affirmance of the Court of Appeals on the ground that the landlord restored the premises as mentioned is reversible error, as we show in Point IV), it will be assumed *arguendo* for the purpose of this point that the record does establish that the landlord restored the premises in the manner stated in the opinion of the Court of Appeals and that the legal effect of the restoration is in issue.

(a) *Reletting After the Tenant's Abandonment of the Premises Does Not Effect a Surrender Under the Law of New Jersey.*

Although at common law and in New York and some other states reletting after the tenant's abandonment of the premises effects an acceptance of a surrender unless the tenant *agrees* to a reletting for the tenant's account (*Gray* v. *Kaufman Dairy & Ice Cream Co.*, 162 N. Y. 388),[1] the general rule in this country is to the effect that in such event the landlord may relet without accepting a surrender and may recover the difference between the rent reserved in the lease and the rent received on reletting, even though the lease contains no provision expressly authorizing the landlord to relet as the tenant's agent. 16 R. C. L. Sec. 672; 13 L. R. A. (N. S.) 398; 3 A. L. R. 1080; Tiffany, Landlord and Tenant (1910) page 1338; Tiffany, Real Property (1920) page 1586. In most jurisdictions following this general rule it is held that the landlord's reletting releases the tenant from further liability unless the landlord notifies the tenant before reletting that he intends to relet for the latter's account. However, in New Jersey (which also follows the general rule), the giving of such notice by the landlord is not a prerequisite to the survival of the tenant's liability,[2] but the party asserting

[1] Under the common law doctrine mere notice by the landlord of intention to relet for the account of the tenant is ineffectual.

[2] The same rule is followed in a number of other states: *Martin* v. *Siegley*, 123 Wash. 683; *Auer* v. *Hoffman*, 132 Wis. 620; *Miller* v. *Benton*, 55 Conn. 529; *Marshall* v. *John Grosse Clothing Co.*, 184 Ill. 421; *J. C. Meyer & Co.* v. *Smith*, 33 Ark. 627; *Scott* v. *Beecher*, 91 Mich. 590; *Sessinghaus* v. *Knocke*, 127 Mo. App. 300; *Guy* v. *Gould*, 126 Kan. 25; *Ralph* v. *Deiley*, 293 Pa. 90; *Bumiller* v. *Walker*, 95 Oh. St. 344 (see *In re Paramount Publix Corp.*, *supra*, at p. 85).

a surrender must, in order to establish it, prove acts of the parties (*other than reletting without notice*) which are inconsistent with the continued existence of the lease. *Liskovsky* v. *Blau, supra; Banks* v. *Berliner,* 95 N. J. L. 267; *Albrecht* v. *Thieme,* 97 N. J. L. 103, aff'd. 98 N. J. L. 249; *Dolton* v. *Sickel,* 66 N. J. L. 492, aff'd. 68 N. J. L. 731.[1] While mere abandonment, whether or not followed by reletting, terminates the *privity of estate* between landlord and tenant in New Jersey (*Whitcomb* v. *Brant,* 90 N. J. L. 245), it does not destroy the *privity of contract* (as does the acceptance of a surrender) and thus does not release the tenant from liability to pay rent.

The Court of Appeals itself recognized that under the New Jersey law reletting without notice did not effect a surrender, saying (R. 73):

> "Apparently proof that a lease was rejected by a receiver in bankruptcy of the lessee, that the lessor re-entered and relet without notice to the lessee of acceptance of surrender or of an intention to relet for the lessee's account, is not sufficient as a matter of law to show a surrender and acceptance of the leased premises. *Liskovsky* v. *Blau,* 114 N. J. Law, 324, 176 A. 562. See, also, *Dolton* v. *Sickel,* 66 N. J. Law, 492, 49 A. 679; *Banks* v. *Berliner,* 95 N. J. Law, 267, 113 A. 321."

Under these circumstances it would seem unnecessary to discuss this phase of the case further. A detailed analysis of the New Jersey decisions, however, may be found in Appendix A.

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[1] Thus, whereas in New York a surrender results in the absence of proof of an agreement to the contrary, in New Jersey a surrender never results unless an agreement to effect a surrender is shown. See also *Mecker* v. *Spalsbury,* 66 N. J. L. 60; *Miller* v. *Dennis,* 68 N. J. L. 320; *O'Neil* v. *Pearse, supra.*

(b) *Restoration of the Premises, Whether or Not Followed by Reletting, Does Not Effect a Surrender Under the New Jersey Law.*

After concluding that reletting without notice after the tenant's abandonment did *not* effect a surrender under the New Jersey law, the Court of Appeals concluded that the landlord's restoration of the premises did, saying (R. 73):

> "But here the evidence went beyond that [re-entry and reletting] and showed that the landlord had made substantial changes in the premises indicative of the resumption of dominion over them inconsistent with the continuing status of landlord and tenant under the lease. These acts together show such an unequivocal breaking off of the relationship which before existed under the lease that the landlord must be held to have accepted a surrender of the premises as a matter of law in consequence of what was done. *Sypherd* v. *Myers*, 80 N. J. Law, 321, 79 A. 340; *Fink* v. *Browe Co.* (N. J. Ch.), 99 A. 926."

The "substantial changes" referred to by the court are those described in an earlier part of its opinion where it is said (R. 72) that the landlord "made structural changes in the premises *to restore them to the condition they were in when leased* by rebuilding a party wall and closing up a common entrance".

The cases cited by the Court of Appeals do not support its conclusion. In the *Sypherd* case it did not appear that any repairs or alterations whatever had been made by the landlord after resuming possession. In the *Fink* case it was held merely that "making changes and alterations therein that were not necessary as repairs for the preservation of the building",

among other acts on the part of the landlord,[1] indicated an intention on the landlord's part to accept a surrender.

The citation of the *Fink* case by the Court of Appeals apparently evidences its belief that the repairs made by the landlord upon resuming possession were not necessary for the preservation of the building. But no such conclusion fairly can be drawn from the skeleton facts found by the Court of Appeals—to wit, that a party wall was rebuilt and a common entrance closed up. In the absence of anything in the record on the subject, the only inference that reasonably can be drawn as to the nature of the repairs is that the landlord upon the debtor's abandonment was compelled to restore the party wall (which the debtor had removed so that it could occupy the premises involved herein and the adjoining premises as one unit) and to close up the common entrance (which the debtor had made) in order to prevent such injury as might result from the separate occupation of the *adjoining* premises either by the debtor or by a new tenant.[2]

The New Jersey decisions clearly hold that repairs made by a landlord upon the tenant's abandonment for the purpose of preserving the premises from injury do not effect a surrender of the lease, even if accompanied by reletting. *Mecker* v. *Spalsbury*,

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[1] The landlord in the *Fink* case also accepted the keys without objection. In the case at bar the keys were not offered to nor accepted by the landlord.

[2] The tenant's alterations had seriously damaged the building. *Cf. Kinney Realty Co.* v. *Salmon*, 106 N. J. Eq. 389; *Agate* v. *Lowenbein*, 57 N. Y. 604; *Woolworth Co.* v. *Nelson*, 204 Ala. 172. The landlord merely repaired the damage.

*supra*;[1] *Liskovsky* v. *Blau, supra; Banks* v. *Berliner, supra; Block* v. *Bell Furniture Co.*, 111 N. J. Eq. 551, 559. The conclusion of the Court of Appeals is, therefore, erroneous in the first place, we submit, on the ground that the repairs made by the landlord were necessary to preserve the building from injury and, therefore, within the doctrine of the foregoing cases.

Assuming, *arguendo,* however, that the repairs made by the landlord in the case at bar were not necessary to preserve the premises under the doctrine of these cases (though this assumption exceeds the realm of reasonableness), it is clear that where the repairs made by the landlord go no further than to restore the premises to their original condition, even though they are not required *to preserve* the premises, such repairs do not effect a surrender, even when accompanied by reletting. *Zabriskie* v. *Sullivan,* 80 N. J. L. 673, aff'd. 82 N. J. L. 545. The Supreme Court said in the *Zabriskie* case (at p. 676):

> "The reparation of the premises by the landlord was also for the benefit of the tenant, for it relieved him of his duty to repair and increased the likelihood of securing a tenant."[2]

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[1] In the *Meeker* case, where a surrender was found, the landlord remodelled the building, which had been leased as a hotel, so that it could be used either as a hotel or for flats. The entire character of the building was thus changed; and, moreover, when the work was begun the premises were already in good condition and repair.

The facts in the *Fink* case do not show what the nature of the repairs were, the opinion merely stating the conclusion of the court that they were not necessary for the preservation of the building.

[2] The lease contained no covenant to repair, but a covenant by the tenant to surrender the premises in good condition at the expiration of the term. Hence, the repairs made were those required to restore the premises to substantially as good a condition as existed at the commencement of the term. The lease in the instant case contains both covenants (R. 27).

The general rule where reletting alone does not effect a surrender, is clearly stated by one writer (Schnebly, Operative Facts in Surrenders, 22 Ill. L. Rev. 117, 129) as follows:

> "Another question which arises is whether or not a surrender results from the fact that the lessor has made repairs before reletting. The making of necessary repairs ought not to be regarded as indicating any particular intention. It is well known that repairs must usually be made when there is a change of tenants; that new tenants will usually demand more than tenants who are settled on the premises. The old lessee is benefited by the making of such repairs if the result is to secure a new tenant more quickly, or to obtain a higher rental than would otherwise be realized. Such repairs do not, therefore, cause a surrender. Where expensive and unnecessary repairs have been made, the question is more serious. Such action on the part of the landlord may make it appear that he has taken advantage of the tenant's default to eliminate him entirely, and to make the premises a source of greater profit to himself. Moreover, the making of extensive alterations means that the premises must stand idle while these alterations are being effected, and that the loss to the tenant may be aggravated."

In the instant case the repairs were neither unnecessary nor extensive enough to prevent reletting for any appreciable period and thus aggravate the tenant's loss. On the contrary, by making the premises rentable, the debtor's damages were mitigated.

Any rule that a landlord could not restore premises to their original condition before reletting would nul-

lify the New Jersey rule that a landlord may relet for the tenant's account, since the privilege is worthless unless the landlord may put the premises in rentable condition. It is apparent that the premises in the case at bar could not have been relet as an independent unit *without four walls* and their own private entrance, and that, therefore, the landlord's repairs were necessary in order to enable her to relet.

The trustee in its brief in opposition to the application for certiorari (at pp. 16, 18) states that it is provided in the lease that "it is only upon termination of the lease that she may restore the alterations made by the debtor". The only reference to the record in support of this assertion is to the covenant in the lease relating to *improvements* (R. 28).[1] This provision merely provided that the lessor might make "such alterations and/or improvements" as it should desire, and that "said *improvements*" (not alterations) should become the property of the lessor "at the expiration or other determination of this lease". Obviously a *removed wall* and *a hole in another wall* were not *improvements* which could become the property of the landlord at any time; and it will be noted that the covenant does not state that the "alterations" made by the lessee shall ever become the property of the lessor.[2]

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[1] The provision reads as follows:

> "And the said lessee further covenants and agrees that it will, at its own expense, make such alterations and/or improvements upon the premises hereby demised as it shall desire, and lessor hereby consents to the making of any such alterations and/or improvements by lessee, *said improvements* to belong to and become the property of the lessor at the expiration or other determination of this lease."

[2] Even if the alterations made by the debtor were "improvements" within the meaning of the provision, the provision would be clearly inapplicable where the debtor abandoned the premises and the so-called improvements, as the debtor and the trustee

Thus, both principle and common sense are opposed to the conclusion of the Court of Appeals that restoration and reletting relieved the tenant from liability on the lease and, we submit, its judgment should be reversed for that reason alone, with instructions to allow the claim, subject to proof of the amount of damages.

## POINT IV.

**The Court of Appeals committed reversible error in affirming on the ground that the landlord restored the premises, for in so doing it decided an issue not raised either by the pleadings or the proof.**

As has been stated, the trustee's objection to the claim (R. 14) raised simply one narrow issue of local law,—to wit, whether the landlord's reentering and reletting terminated the debtor's liability under the lease. It contained no allegation that the landlord had restored the premises to their former condition before reletting, nor that the restoration had the effect under the New Jersey law of effecting a surrender. The stipulations of fact, which were drawn in the light of the sole issue raised by the trustee's objection, did not stipulate that the landlord had so restored the premises nor that she had filed a claim for the expense of restoration.

Even if it be assumed that the Special Master had the right to take judicial notice of the fact that the

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did in the case at bar. The abandonment would constitute a waiver by the debtor of its rights under the clause in question. In any event, it would not follow that the restoration of the premises would effect a termination of the lease. The only result would be the liability of the debtor for the conversion of the improvements. Under the New Jersey law, it must be remembered, the landlord was clearly authorized to relet for the account of the tenant upon his abandonment.

landlord had filed a claim in the prior bankruptcy proceeding for the expense of restoration, although he was not requested to do so by any party at any time (R. 17, 18),[1] the "finding" of the Master was simply that the landlord had *filed* such a claim. His conclusion from this finding was that the filing of such a claim indicated that the landlord thought the lease had been terminated by her previous reentry and reletting because the debtor was [as the landlord alleged in her proof of claim] under no obligation to restore until the *expiration* of the term (R. 41).[2] He did not consider the restoration itself as a factor bearing on the question of whether a surrender had been effected. His report was limited to the question raised by the objection to the proof of claim and the stipulated

[1] The Special Master's report (R. 41) mentions that the "Trustee may well point to" the filing of the claim for restoration in support of its position. Actually, however, the trustee did not refer, at the hearing or in the brief submitted to the Master, to the filing of such a claim nor to the restoration. The Master, *so far as the report shows*, did not purport to take judicial notice of the filing of the claim, but referred to it, apparently, because of the personal knowledge he had acquired in acting as referee in bankruptcy in the prior bankruptcy.

The report also states (fol. 123) that "the stipulation herein shows that this claim [for restoration] is also asserted in this Reorganization proceeding", but the Master was mistaken as to this, as the two stipulations of fact (R. 19, 33) contain no reference to the filing of a claim for restoration, either in the bankruptcy proceeding or in the reorganization proceeding.

[2] This conclusion, which was not approved by the Court of Appeals, was erroneous, since the claim was provable, if at all, only on the theory that the bankruptcy petition constituted an anticipatory breach of the agreement to restore, not that the lease had actually *expired* or been terminated at a later date. *In re Metropolitan Chain Stores*, 66 F. (2d) 485, 487; *Possart* v. *Irving Trust Co.*, 69 F. (2d) 807. That this was the theory on which the proof of claim was filed is shown by the allegation in the proof of claim that "the lease has now expired *by reason of the bankruptcy*". [If it is proper to take judicial notice of the proof of claim, the allegations therein are clearly probative of the theory on which the claim was based.]

facts. The opinion of the District Court was similarly limited (R. 49).

The Court of Appeals, however, seized on the Master's finding that a claim for reimbursement of the expense of restoration had been filed and drew from it inferences of further facts,—to wit, that the repairs made by the landlord upon resuming possession were "structural changes" (R. 72) and, by implication, were not necessary for the preservation of the premises or in order to relet.

The Court of Appeals departed from the usual course of judicial procedure in "finding" that the landlord had actually restored the premises and in making certain inferences of fact in regard to the exact nature of the repairs made by the landlord. Even if the proof of claim for the expense of restoration should be deemed to be a part of the record on the issue raised by the proof of claim now before the Court, as though introduced into evidence by the trustee at the hearing before the Master, the proof of claim obviously would not be probative of the truth of the facts alleged therein,[1] any more than facts can be proved against a plaintiff by introducing a copy of his complaint in *another cause of action.*

Moreover, if the trustee's objection had raised the issue that the landlord's action in making certain repairs had effected a surrender and had introduced proof in substantiation of that objection, the petitioner could have proved the details with respect to the exact nature of the repairs made by the landlord and with respect to whether they were necessary to preserve the premises from injury after the debt-

[1] Therefore, the petitioner would have been entitled to controvert any fact stated in that proof of claim.

or's abandonment or to make them rentable. If the record had definitely shown that they were necessary to preserve the premises or to make them rentable, the Court of Appeals must have held, as we have seen from the authorities cited in Point III, that no surrender had been effected.[1] All these considerations were ignored by the Court of Appeals when it decided this question without pleadings and without evidence and without the question having been passed upon by the Special Master or the District Court.[2]

In thus proceeding the Court of Appeals has ignored the elementary principle that appellate courts should limit their decisions to issues properly framed and passed upon by the courts below, and to evidence regularly produced. *Liberty National Bank* v. *Bear*, 265 U. S. 365; *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200; *Helvering* v. *Salvage*, 297 U. S. 106; *Compania General* v. *Collector*, 279 U. S. 306.

The *Liberty National Bank* case, *supra*, is precisely in point. This Court there held that where neither the trustee's objection to a claim nor the proof introduced by it raised an issue of law, the Court of Appeals could not base its affirmance of an order disallowing the claim on such issue, but should

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[1] As it was, the Court of Appeals ignored the fact that the Master *did not* find, although as referee in the prior bankruptcy proceeding he must have known the facts regarding the restoration, that the repairs made by the landlord were of such a nature as to change the character of the premises and thus effect a surrender by operation of law (*cf. Meeker* v. *Spalsbury*, *supra*).

[2] The trustee in its brief in opposition to the application for certiorari asserted (pp. 16, 17) that the Master found "that the alterations made by the Debtor had in fact been restored by the landlord" and that the petitioner did not except to "that finding". Since no such finding was made (R. 41), the petitioner could not except thereto. The exception was fully as broad as the "finding" made by the Master (R. 44, par. 5).

have reversed. The trustee had objected to the claim on the ground that the judgment securing it had been recovered within four months prior to bankruptcy, but it had not alleged, nor had it proved, that the bankrupt was insolvent at that time. Similarly, in the case at bar, the trustee neither alleged nor proved the landlord had made any repairs, nor did it allege that the making of such repairs had effected a surrender.

As this Court said in the *General Utilities* case, *supra* (p. 206):

> "Stipulations concerning facts and any other evidence properly are accommodated to issues adequately raised."

This Court in that case held that the Court of Appeals should not have decided the case upon a ground not presented to nor ruled upon by the Board of Tax Appeals, particularly when it had, in support of its decision, made certain inferences of fact in conflict with the stipulated facts.

It is thus clear that the Court of Appeals committed reversible error in *affirming* the judgment below. The only question that remains, therefore, is whether the judgment should be reversed with instructions to allow the claim, subject to proof as to the amount of damages, or reversed with instructions for a new trial.

The Court ought not to grant a new trial in the case at bar in view of the submission of the case on an agreed statement of facts drawn in the light of the trustee's objection.[1] Even in an action at law,

[1] Stipulations are designed to restrict issues or settle disputed facts, or both, and are binding unless cause is shown for setting them aside. *Brooklyn Mining Co.* v. *Miller*, 227 U. S. 194, 201; *United States* v. *Davison*, 1 F. (2d) 465, 469, 470; *Schmertz Wire Glass Co.* v. *Continuous Glass Press Co.*, 216 Fed. 828; *McNeill* v. *Town of Andes*, 40 Fed. 45.

where the Seventh Amendment is applicable, an appellate court will, upon a reversal of a case submitted upon an agreed statement of facts, direct the entry of final judgment without remanding for a new trial. *Thomas* v. *Matthiessen,* 232 U. S. 221, 236; *United States* v. *Illinois Surety Co.,* 226 Fed. 653, 664 (C. C. A. 7); *Massachusetts Bonding & Ins. Co.* v. *Santee,* 62 F. (2d) 724, 728 (C. C. A. 9); *Maryland Casualty Co.* v. *Beebe,* 54 F. (2d) 743, 746. The Court should, therefore, we submit, reverse with instructions to allow the claim, subject to proof as to the amount of damages.

In any event, if every other contention of the petitioner be denied, the Court should direct a new trial. In such an event, if the stipulations are not binding, or are binding only to the extent of the facts covered, both parties can introduce additional evidence as to the nature of the repairs and the necessity therefor, provided the district court permits at this late date the trustee to amend its objection to the claim.

Other relevant facts might be established on a new trial. Though the record in the case at bar shows by negative implication that the petitioner did not execute an assignment agreement such as those involved in *Otis* v. *Irving Trust Co.* (No. 436), it does not show that one was *offered* to the petitioner. However, the opinion of the Court of Appeals in the *Otis* case states (83 F. (2d) 202, 203-4) that the trustee made it a practice to offer to landlords whose leases were burdensome an agreement providing for an express surrender, in return for the execution of a release of all claims against the trustee, the bankrupt estate and the debtor (see also Record in No. 436, pp. 43-65). On a new trial the petitioner will be permitted to prove whether or not such an agreement was offered

to the landlord in the case at bar and declined. The fact that the landlord was offered and declined such an agreement, if proven, would conclusively show that she neither intended nor desired to accept a surrender or otherwise terminate the debtor's liability under the lease.

### *Conclusion*

The judgment of the Court of Appeals should be reversed, with instructions to allow the petitioner's claim in the amount of such loss as the petitioner may prove to have been incurred, subject to the limitation provision as construed by this Court in *Kuehner and Fischer* v. *Murphy, et al.* (No. 354).

Respectfully submitted,

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## Appendix A.

### THE NEW JERSEY DECISIONS ESTABLISH THAT A LANDLORD MAY RELET FOR A TENANT'S ACCOUNT WITHOUT NOTICE.

In *Liskovsky* v. *Blau,* 114 N. J. L. 324, the highest court of New Jersey held that mere reletting by a landlord after the tenant's abandonment of the premises, in the absence of other evidence, is, as a matter of law, a reletting for the tenant's account, and that it does not effect a surrender.[1] So far as the facts set forth in the opinion in that case show, the lease contained no special covenant, and the landlord gave no notice to the tenant that he intended to relet for the tenant's account.

The contention made by the trustee in the Court of Appeals, which was rejected by that court, that the fact that the *record on appeal* in the *Liskovsky* case showed that the lease contained a clause expressly permitting the landlord to relet as agent for the tenant indicated that the court's decision was restricted to leases containing such special clauses, is not tenable. The court did not mention the special clause among the facts stated in its opinion. It is clear, therefore, that it chose to lay down a broad rule, rather than to base its decision on the narrow ground that the lease before it contained such a clause.[2]

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[1] The appellate court affirmed an order of the trial court directing a verdict in favor of the landlord, it appearing that the landlord had relet in his own name after the tenant and its receiver in bankruptcy had abandoned the premises.

[2] Moreover, it is well known that decisions and principles of law are applicable only to the facts stated in the opinion. *Utah Consolidated Lighting Co.* v. *Apex Mining Co.*, 285 Fed. 249, 256, cer. den. 261 U. S. 617; *Moriarty* v. *City of New York*, 132 App. Div. 10, 12, aff'd 197 N. Y. 544; *Yoders* v. *Township of Amwell,* 172 Pa. St. 447, 450; 7 R. C. L. 1003.

The broader ground of decision announced by the New Jersey

The broad rule laid down merely followed prior New Jersey decisions. *Banks* v. *Berliner*, 95 N. J. L. 267; *Albrecht* v. *Thieme*, 97 N. J. L. 103, aff'd. 98 N. J. L. 249.

In *Banks* v. *Berliner* the landlord upon the tenant's abandonment notified him that she would hold him liable for the rent, which evidenced that she did not, *by reentering*, intend to accept a surrender, but she did not notify him that she intended *to relet* for his account. Sometime thereafter it appeared that the landlord tried to relet the premises to others, and the tenant contended that the landlord's efforts had effected a surrender. It was held that the efforts to relet did not effect a surrender, and the court stated that "if she had succeeded in reletting the property, the tenant would have been entitled to have credited on his obligation the amount received under the new lease", citing *Whitcomb* v. *Brant*, 90 N. J. L. 245. Not only did the court not indicate that before making a new lease the landlord would have been required to notify the tenant that she was reletting for his account, but the citation of *Whitcomb* v. *Brant* clearly indicates that the court was of the opinion that the tenant's continued liability was not conditioned on such notice, for the opinion in the *Whitcomb* case clearly indicates that, if the landlord had been suing the tenant (instead of the tenant suing the landlord for the increased rental resulting from reletting), the tenant would have continued liable for the difference

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court may not be considered a dictum, since it appears to have been the actual ground of the decision. But even if it were a dictum to the extent that it applies to leases containing no special clauses, the dictum under the New Jersey law must be accepted as announcing the New Jersey rule in the absence of any decisions to the contrary. *Kutschinski* v. *Thompson*, 101 N. J. Eq. 649, 660.

between rent reserved and the avails of reletting, although the landlord had not notified the tenant that she was reletting for his account.[1]

In *Albrecht* v. *Thieme*, 97 N. J. L. 103, aff'd. 98 N. J. L. 249, the landlord upon the tenant's abandonment also indicated that he did not intend to accept a surrender, by advising the tenant that he would hold him accountable for any loss which he might sustain, but when he subsequently relet the premises he did not notify the tenant that he was reletting for the tenant's account. The court did not even consider whether the subsequent reletting without notice had effected a surrender, but proceeded to consider whether the reletting constituted an *eviction* of the tenant. The court concluded that there was no actual eviction because the tenant had abandoned and said (at p. 105):

> "Where, however, the tenant has vacated and abandoned the premises, an eviction by a re-letting is constructive merely and should, within the reason of the rule, impose upon the landlord no penalty other than that of crediting the tenant with the sum so earned by the property during the term."

To the same effect is *Dolton* v. *Sickel*, 66 N. J. L. 492, aff'd. 68 N. J. L. 731.

The leases involved in the *Berliner*, *Albrecht*, and *Dolton* cases did not contain any special covenant authorizing reletting for the tenant's account. Thus, under the New Jersey authorities there is no substantial difference, as far as the point now under discussion is concerned, between a lease which contains a

[1] Although the lease in the *Whitcomb* case contained a covenant expressly authorizing the landlord to relet upon the tenant's abandonment, the court did not base its dictum on this factor.

clause expressly authorizing reletting by the landlord as agent for the tenant, or which provides that the landlord may relet and apply the avails to the rent due under the first lease (as in *Whitcomb* v. *Brant, supra, Meeker* v. *Spalsbury,* 66 N. J. L. 60, and *Jones* v. *Rushmore*, 67 N. J. L. 157), and a lease which contains no special clause whatever in regard to reletting. In short, a reletting standing alone never effects a surrender under the New Jersey law, but merely constitutes what is called a constructive eviction, the only legal effect of which is to require the landlord to credit the tenant with the avails of reletting.[1]

In every New Jersey case in which it was held that a surrender had been effected, it appeared that something had been said, or something done (other than mere reletting without notice), which was considered inconsistent with the continued relationship of landlord and tenant and which thus evidenced a mutual agreement that the lease should be terminated, such as use of the premises by the landlord for his own purposes (*Lorenz* v. *McCloskey,* 135 Atl. 350; (*Sypherd* v. *Myers,* 80 N. J. L. 321), or the making of alterations by the landlord upon his reentry which completely changed the character of the premises (*Meeker* v. *Spalsbury, supra*) and indicated that the landlord had initiated a venture of his own.

In analyzing the New Jersey decisions it is appropriate that this Court should consider that the presence or absence in a lease of a special clause authorizing reletting has no logical bearing on the question of whether or not the landlord must notify the tenant of his intention to relet for the tenant's account.

[1] For a criticism of the rule that reletting constitutes constructive eviction, see Tiffany, Landlord and Tenant, p. 1276.

Even when there is such a clause in a lease, the landlord, of course, is not obligated to relet as agent for the tenant but may accept the proffered surrender and relet solely for his own account. Consequently, whether or not the lease contains such a covenant, the question in each case is whether the landlord intended to relet for the tenant's account or for his own account.

The most that can be said in favor of the requirement of notice to the tenant that the landlord intends to relet for the tenant's account is that it compels a disclosure of the landlord's intention at the time of reletting. If there is any merit in this requirement it applies equally as well where the lease contains such a clause as where it does not.[1]

It will be observed that, from the point of view least favorable to the petitioner, there is no New Jersey decision holding that a tenant was released merely because the landlord after abandonment relet without notice. Consequently, in that view of the matter, this Court must decide the question of surrender according to its own views of the law of landlord and tenant. *Thorley* v. *Pabst Brewing Co.*, 179 Fed. 338, 339. The rule permitting reletting for the tenant's account, even in the absence of a special covenant, is

[1] If it is relevant that the record in the *Liskovsky* case shows that the lease expressly authorized reletting as agent, then it is also relevant to point out that the record in that case shows that the landlord did *not* notify the tenant that he was reletting for the latter's account, and that there was no evidence as to the landlord's intention in reletting, except the landlord's own testimony that he intended to relet for the tenant's account, although this intention was not communicated to the tenant or to the latter's sureties (State of Case, pp. 80, 97-8). That the court did not attribute importance to the mere undisclosed intention is clearly indicated in its opinion: "* * * There is no proof in the case that plaintiff was acting for the Zimmerman Furniture House, Incorporated [the tenant], when this new lease was made.* * *"

the one which best accords with fairness and public policy.[1]

Whatever could be said for a rule conditioning reletting for the tenant's account upon prior notice to the tenant, there can be no justification for applying such a rule to a corporate tenant which has been adjudicated a bankrupt. The bankrupt corporation, stripped of its assets, would not be concerned with the claim which the landlord would have if the premises should be relet at a loss, or for less than they could have been relet for, and neither the trustee in bankruptcy nor the bankrupt corporation would have the right in New Jersey to recover any over-plus from the landlord if the premises should be relet at a profit, in the absence of a provision in the lease requiring the landlord to account for any such over-plus (*Whitcomb* v. *Brant, supra*). A demand on a bankrupt corporation or its trustee in bankruptcy after rejection for rent or damages would be futile. A notice of reletting for the bankrupt's account would be as little helpful.[2]

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[1] As the Supreme Court of Washington said in *Martin* v. *Siegley, supra*, 123 Wash. 683, 687:

> "It is not in accordance with public policy to lay down a rule whereby the landlord would be required to permit the premises to remain idle over a long term and thereafter recover damages for the full amount of the rentals stipulated for the term, because *it is better for the parties to the agreement, as well as to the public, to have property put to some beneficial use.*"

[2] *Cf.*, the decision of the court below in *In re Mullings Clothing Co.*, 238 Fed. 58, where it was held that a surrender had not been effected under Connecticut law by the landlord's reletting without notice after rejection of the lease by a receiver of the tenant appointed in a dissolution proceeding, although the lease contained no special clause and although no precedent existed under the applicable state law for its decision. In *Miller* v. *Benton*, 55 Conn. 529, cited by the court, it appeared that the landlord twice notified the tenant he would hold him liable for the rent, but no such notice was given in the *Mullings* case.

The Special Master's reasoning in support of his conclusion that a surrender had been accepted (apparently concurred in by the District Court at R. 50) is entirely unsupported, either by authority or principle, and was, as we have seen, rejected by the Court of Appeals:

1. The new lease was not required to recite that the landlord was acting for the tenant (*Liskovsky* v. *Blau, supra*), and no notice was required to be given to the tenant under the authorities cited, which the Master entirely ignored and failed to discuss (R. 40).

2. The Master concluded (R. 40) that because the landlord had no provable claim in bankruptcy it was unlikely for her not to have resumed control of the premises for her own benefit. This presumption of the landlord's intention is inconsistent with the decision of the New Jersey Court of Errors and Appeals in the *Liskovsky* case, where the tenant was also a bankrupt corporation. Moreover, the presumption indulged by the Master is unjustified as a matter of common sense, for there is nothing to justify a presumption that the landlord intended to accept a surrender and terminate the debtor's liability on the lease, since she had nothing to gain by so doing. Under the New Jersey law, even if the landlord succeeds in reletting at a profit, the tenant is not entitled to the profit in the absence of an express provision in the lease (*Whitcomb* v. *Brant, supra*). Thus, in New Jersey there is no reason whatever why the petitioner should have intended to accept a surrender.

3. The Master's conclusion from the filing of a claim for restoration has already been discussed (*supra*, p. 53).

Thus every reason given by the Master for his conclusion is based on an erroneous conclusion of law or an unwarranted assumption of fact. His report and the opinion of the District Court, failing as they do to cite or consider a single New Jersey authority, or, for that matter, any other authority (R. 37-42, 49), are entitled to little weight.